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No. _____

In The

Supreme Court of the United States

October Term, 1982

—o—

THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION

Respondents.

—o—

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF MONTANA

—o—

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QUESTION PRESENTED FOR REVIEW

Whether The State of Montana Can Include Interest Income From Certain Federal obligations (*i.e.*, 31 U.S.C. §769 and 12 U.S.C. §§1433, 1725(e), 2055, 2079, 2134), in the net income measurement of the Montana Corporation License Tax imposed by Sections 15-31-101 *et seq.*, Montana Code Annotated.

A. Whether the Montana Corporation License Tax Satisfies the Requirements of the Exception Contained in 31 U.S.C. §742, so as to Allow the Inclusion of Federal Interest Income Within the Computation of its Tax Base.

B. Whether the Immunity From State Taxation Described in 31 U.S.C. §769 and 12 U.S.C. §§1433, 1725(e), 2055, 2079, 2134 is Broader than that Otherwise Provided by 31 U.S.C. §742.

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Respondents.

—o—

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF MONTANA

—o—

The Petitioner, the State of Montana, respectfully prays that a Writ of Certiorari issue to review the judgment and opinion of the Supreme Court of Montana entered in this case.

OPINION BELOW

The Opinion of the Montana Supreme Court is reported at *First Federal Savings & Loan Association v. Department of Revenue*, ____Mont.____, 654 P.2d 496 (1982). A copy of the Opinion of the Montana Court appears in the Appendix, pp. 1a-10a.

JURISDICTION

The Opinion of the Montana Supreme Court was entered on September 23, 1982. A timely Petition for Rehearing was denied by a split court on December 6,

1982, Appendix pp. 11a-12a, and this Petition for Certiorari was filed within 90 days of that date. Accordingly, this Petition is timely under 28 U.S.C. §2101(c) and Supreme Court Rule 20.

The jurisdiction of this Court is invoked under 28 U.S.C. §1257(3).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This case concerns the tax exception contained in 31 U.S.C. §742. Also involved are certain provisions of the Montana Corporation License Tax, in particular §§15-31-101(3), 15-31-143(1) and 15-31-113(1)(a)(i), of the Montana Code Annotated. The following statutes are also involved in this case, but because of their length are set out verbatim in the Appendix, pp. 34a-36a: 31 U.S.C. §769 (United States Treasury Bills); 12 U.S.C. §§ 1433 (Federal Home Loan Bank Notes), 1725(e) (Federal Savings & Loan Insurance Corporation Notes), 2055 Federal Land Bank Obligations), 2079 (Federal Farm Credit Bank Securities), and 2134 (Federal Home Loan Stock Dividends).

31 U.S.C. §742:

> Exemption From Taxation
>
> Except as otherwise provided by law, all stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations and except estate taxes or inheritance taxes.

Montana Code Annotated:

15-31-101. Organizations subject to tax

* * *

(3) Every corporation, except as hereinafter provided and except as provided in 33-2-705(6), engaged in business in the State of Montana shall annually pay to the state treasurer as a license fee for the privilege of carrying on business in this state such percentage or percentages of its total net income for the preceding taxable year at the rate hereinafter set forth. In the case of corporations having income from business activity which is taxable both within and without this state, the license fee shall be measured by the net income derived from or attributable to Montana sources as determined under part 3. This tax is due and payable on the 15th day of the 5th month following the close of the taxable year of the corporation; however, the tax becomes a lien as provided in this chapter on the last day of the taxable year in which the income was earned and is for the privilege of carrying on business in this state for the taxable year in which the income was earned.

15-31-143. Return and payment on corporate dissolution. (1) It is hereby declared that the policy of the State of Montana, both at the time of the enactment of the corporation license tax law and at all times since, has been and still is that every corporation doing business in Montana shall pay an excise tax for the exercise of such privilege and that the amount of such tax shall be based upon the total taxable net income of such corporations during the entire period of time they are engaged in business in this state. No remission of that obligation for the last year in which a corporation engages in business in Montana was intended by the original enactment of this section.

15-31-113. Gross income and net income. (1) The term "gross income" means all income recognized in determining the corporation's gross income for federal income tax purposes and: (a) including: (i) interest exempt from federal income tax;

STATEMENT OF THE CASE

Respondents, First Federal Savings and Loan Association of Missoula and Havre Federal Savings and Loan Association are federally chartered savings and loan associations doing business in the State of Montana in corporate form. As such, Respondents are subject to the Montana Corporation License Tax provided for in Title 15, Chapter 31 of the Montana Code Annotated (MCA).

In their respective corporation license tax returns for tax year 1979, Respondents deducted the interest income derived from certain federal obligations from their gross income to arrive at net income for purposes of measuring the Montana Corporation License Tax. Subsequently, Petitioner, the Montana Department of Revenue audited the returns, disallowed the deduction taken for interest income on certain United States obligations and issued notices of resulting tax deficiencies.

Thereafter, Respondents filed suit in the District Court of the First Judicial District of the State of Montana for the County of Lewis and Clark, contending in their complaint for Declaratory Judgment as follows:

> 16. Plaintiffs contend that while 31 U.S.C. Section 742, as a general rule, authorizes the inclusion of interest income from United States obligations in the calculation of net income for purposes of a nondiscriminatory corporation license tax, this federal statute does not repeal, amend, nullify or control the specific federal statutes relating to the federal securities listed on "Exhibit A" wherein it is provided that the interest income from these securities is specifically exempted from any form of state taxation which would include corporation license taxes.
>
> 17. The federal statutes pertaining to the federal securities shown on "Exhibit A", being more specific than the general statute regarding state taxation of interest income from obligations of the United States must be, and are,

controlling in determining whether the interest income from such securities is taxable.

In answer to the Respondents' Complaint, the Montana Department of Revenue contended that the inclusion of interest income from federal obligations in the net income measurement of a corporation franchise tax is permissible under the express language of 31 U.S.C. §742 and pursuant to a long line of decisions of this Court interpreting the exemption language of §742 as not extending to a nondiscriminatory franchise tax.

The Respondents never questioned that the Montana Corporation License Tax is anything other than an excise tax on the corporate franchise. See Items 13, 15 and 18 of Complaint, Appendix, pp. 38a-50a.

Pursuant to the filing of a Motion for Summary Judgment by each party the trial court held that interest income from the specified federal obligations were includable in the computation of the Montana Corporation License Tax pursuant to 31 U.S.C. §742 as well as the established line of case law emanating from this Court interpreting this section, and entered judgment on behalf of the Petitioner.

The Memorandum and Order of the District Court appears in the Appendix at pp. 13a-27a.

The Respondents herein appealed the order of the District Court to the Montana Supreme Court which reversed and held that the inclusion of the interest income from the specified federal obligations in the net income measurement of the Montana Corporation License Tax violated both 31 U.S.C. §742 and the federal agency statutes providing for issuance of such obligations (31 U.S.C. §769; 12 U.S.C. §§1433, 1725(e), 2055, 2079, and 2134). In reaching that conclusion the Montana court declined to address, discuss or recognize the 100 plus year

interpretation given to the exemption language contained in 31 U.S.C. §742 by this Court, upholding inclusion of federal interest income in the measure of a state franchise tax.

A second issue presented to the Montana Supreme Court by the Respondent but left undecided was whether the Montana Corporation License Tax is discriminatory. The Montana Court determined this second issue to be moot in light of its decision on the first issue, 654 P.2d at 499, however it will be addressed in this Petition. The Montana Court also addressed a third issue concerning the application of a 1979 legislative amendment to the net loss carryover provisions of the Montana Corporation License Tax statutes. This third issue being solely a matter of state law is not raised into issue in this Petition.

REASONS FOR GRANTING THE WRIT OF CERTIORARI

A. THE MONTANA SUPREME COURT'S DECISION ON THE FEDERAL QUESTION CONFLICTS WITH APPLICABLE DECISIONS OF THIS COURT AND OTHER STATE COURTS OF LAST RESORT.

INTRODUCTION

This Court issued a decision on January 24, 1983 in *Memphis Bank and Trust Company v. Riley C. Garner*, ____U.S.____, 51 U.S.L.W. 4104, which held a Tennessee franchise tax law imposing a 3% tax on the net earnings of banks doing business within the state, unconstitutionally discriminatory under the Supremacy Clause. The rationale of this Court's holding was that although interest income from federal obligations is includable in certain instances in the base of the tax, since interest income from otherwise comparable state and local obligations was excluded therefrom the state tax was

discriminatory. The issue now presented to this Court for review was not directly addressed in *Memphis Bank and Trust Company* but was specifically referred to and set forth in Footnote 5 to the Opinion, 51 U.S.L.W. at 4105, as follows:

> In establishing the Federal Credit Banks, Congress made clear that the obligations of these banks would be immune from taxation by the States. 12 U.S.C. §§2055, 2079 and 2134. We have no occasion to determine whether the immunity described in these provisions is broader than that otherwise provided by 31 U.S.C. §742. . . .

This Court now has the opportunity to directly address this particular issue which possesses significant import for not only the State of Montana and its citizens, but all states which levy a "nondiscriminatory franchise tax or other nonproperty tax in lieu thereof on corporations" and include in the measure of such tax interest income from otherwise tax exempt federal obligations. In addition, this issue affects more than 120 years of jurisprudence from this Court in the federal and state franchise taxation area.

If the issue is left unaddressed, states such as Montana will continue to endure the dilemma of finding a method which effectively taxes financial institutions engaged in business within the state so as to truly reflect such institutions' fiscal responsibilities to the state and more importantly to its fellow citizens. Historically, this has been an ongoing and frustrating problem for the State of Montana. See, *Montana Bankers Association v. Montana Department of Revenue*, 177 Mont. 112, 580 P.2d 909 (1978) (holding that the 1959 congressional amendment to 31 U.S.C. §742 prohibits the inclusion of the value of federal obligations in the assets of a national bank for purposes of computing a bank shares tax).

Section 742, after being amended in 1959, was marked by an absence of litigation for more than 20 years. The

Montana Supreme Court's interpretation of 31 U.S.C. §742 in the *Montana Bankers Association* case *supra*, appears to be one of the first state court decisions since the amendment on what was thought to be a settled issue. Since then however, numerous cases relating to that specific issue have arisen. It must be noted the issue has not been resolved uniformly since the highest courts in these states have opted for an interpretation of 31 U.S.C. §742 *contra* to that of the Montana Court. Cf.: *Bartow County Bank v. Bartow County Board of Tax Assessors*, 285 S.E. 2d 920 (Ga. 1982), *appeal docketed*, No. 81-1834, 51 U.S.L.W. 3023 (April 5, 1982) (holding Georgia bank shares tax consistent with 31 U.S.C. §742); and also *Bank of Texas v. Childs*, 615 S.W. 2d 810 (Tex. 1981), cert. granted sub nom. *American Bank and Trust Co. v. Dallas County*, ____U.S.____, 51 U.S.L.W. 3339 (1982) (No. 81-1717) (holding that the State of Texas' property tax on bank shares which is computed on a bank's net assets without any deduction for tax-exempt United States obligations owned by a national bank is not violative of 31 U.S.C. §742).

As can be noted, the effects of the Montana Supreme Court's construction of 31 U.S.C. §742 are beginning to surface in this Court in the bank shares tax area and are requiring the attention of this Court to settle. Now, this unprecedented interpretation of 31 U.S.C. §742 threatens to permeate the area of state franchise taxation. If left unaddressed from this Petition, the Montana Supreme Court's interpretation of 31 U.S.C. §742 will once again pervade the courts of other states and ultimately wind themselves to this Court. This Court can speak definitively on this most important issue by granting this Petition.

DISCUSSION

The decision of the Montana Supreme Court that interest income from certain federal obligations is not in-

cludable in net income for purposes of calculating the Montana Corporation License Tax (which is a franchise income tax), is in derogation of the long established judicial interpretation of 31 U.S.C. §742 developed by this Court, affirming the inclusion of otherwise tax exempt obligations or interest therefrom in the measure of a corporate franchise tax pursuant to 31 U.S.C. §742. In addition, the decision of the Montana Supreme Court is contrary to the recorded congressional intent enacting the 1959 amendment to §742.[1] *See, also,* Symons, *State Taxation of Banks: Federal Limitations*, 99 Banking L.J. 817 (1982).

The issue before the Court in this petition involves the question of when a state can levy a tax involving obligations of the United States. Initially, any state tax must meet the requirements of the exception contained in 31 U.S.C. §742 which expressly provides that such state taxation must first be nondiscriminatory and second must be either a "franchise tax" or "other nonproperty tax in lieu thereof imposed on corporations".[2] It is after these two requirements are satisfied that the subsequent federal issue of this Petition presents itself, *i.e.*, the interpretation to be given to exemption language contained in the federal agency statutes.

The holding of the Montana Supreme Court in this matter ignores the historical treatment of state excise taxation by this Court and fails to recognize that under certain parameters federal interest income can be legally embraced in state taxation according to 31 U.S.C. §742. The

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1. *See*, S.Rep. No. 909, 86th Cong., 1st Sess., reprinted in 1959, U.S. Code Cong. & Ad. News, 2769, 2773-74, and 2777.

2. 31 U.S.C. §742 also excepts "estate taxes or inheritance taxes" but are not at issue in this Petition.

statute under consideration, 31 U.S.C. §742 was enacted in 1862 and provided that "all stocks, bonds, and other securities of the United States held by individuals, corporations, or associations within the United States shall be exempt from taxation by or under state authority." Act of Feb. 25, 1862, Ch. 33, §2, 12, Stat. 346.

An initial reading of the express words of the statute appeared to indicate an all encompassing prohibition of any state taxation which utilized federal obligations or interest therefrom. However in early watershed decisions, this Court clarified construction of the statute and sanctioned certain areas of exception regarding state taxation, thereby curtailing an overly broad interpretation of §742. Two general areas regarding the taxation of state granted privileges have been recognized by this Court as being allowable, notwithstanding the prohibition of §742. The two areas of allowable taxation are the franchise and inheritance tax areas, in which the state levies a tax for the respective privileges of doing business within the state, *Society for Savings v. Coite*, 6 Wall. 594 (1867); *Provident Institution for Savings v. Massachusetts*, 6 Wall. 611 (1867); *Hamilton Co. v. Massachusetts*, 6 Wall. 632 (1867), and transmitting or receiving of property via a testamentary or intestate devise, *Plummer v. Coler*, 178 U.S. 115 (1900).

Congress amended 31 U.S.C. §742 in 1959 so as to expressly ratify and thereby reinforce the judicially developed exceptions to the state taxation exemption contained in §742. The amendment enumerated two requirements which must be satisfied in order to qualify as an exception to the §742 state taxation exemption. The tax must first be either a "franchise tax" or "other nonproperty tax in lieu thereof" imposed on corporations. Subsequent to the 1959 amendment this Court upheld a franchise tax utilizing a net income measure that included

interest income from federal obligations. *See, Reuben L. Andersen-Cherne, Inc. v. The Commissioner of Revenue of Minnesota*, 423 U.S. 886 (1975) (Appeal dismissed for lack of a substantial federal question, and thus constituting a disposition on the merits of the case and concomitantly binding precedent for all courts. *See, Hicks v. Miranda*, 422 U.S. 332 (1975)). Secondly the tax must be "nondiscriminatory". *See, Memphis Bank and Trust, supra*. The Montana Corporation License Tax fulfills both of these requirements.

The Montana Corporation License Tax constitutes a "franchise or other nonproperty tax in lieu thereof imposed on corporations" within the meaning of 31 U.S.C. §742. Montana statutes expressly describe the tax as a license fee for the privilege of carrying on business within the state in corporate form. *See*, §§15-31-143(1) and 15-31-101(3), MCA, *supra*. The Montana Supreme court has held innumerable times that the corporate license tax is a franchise tax upon the privilege of doing business in the State in a corporate capacity. *Montana Bank v. Casey*, 135 Mont. 104, 337 P.2d 935 (1959); *State v. J. C. Maguire Const. Co.*, 113 Mont. 324, 125 P.2d 433 (1942); *O'Connell v. State Board of Equalization*, 95 Mont. 91, 25 P.2d 114 (1933); *East Helena State Bank v. Rodgers*, 73 Mont. 210, 236 P. 1090 (1925); *Cottonwood Coal Co. v. Junod*, 73 Mont. 392, 236 P. 1080 (1925); *Equitable Life Assur. Co. v. Hart*, 55 Mont. 76, 173 P. 1062 (1918). As already noted the Respondents never questioned the nature of the Montana corporation license tax in their Complaint[3] or otherwise and conceded in their

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3. *See, generally*, Respondent's Complaint, reproduced in Appendix, pp. 38a-50a.

Complaint[4] as well as in their briefs[5] to both the Montana Supreme Court and the State District Court that the tax was a franchise tax.

The Montana Supreme Court described the tax in its Opinion issued in this matter as follows, 654 P.2d at 498:

> The Department argued that the Montana Corporation License Tax is a franchise tax on the privilege of doing business in Montana with the tax based upon or measured by the net income of the taxpayer. Hence, it was argued, that the tax is not on the property (interest income) but is on the privilege. This Court finds the argument to be unpersuasive. It is a distinction without a difference in our opinion. *If the franchise tax is on the privilege and the tax is based on the net income, this Court concludes that the tax is on the privilege and the net income.* If the net income includes tax-exempt interest, the tax is on the exempt income which is prohibited by the specific federal statutes creating the federal obligations and granting the tax exemption.

It appears clear that the Montana corporation license tax is a franchise tax. However, if the tax is somehow construed not to be a franchise tax, at very least it is a "non-property tax in lieu thereof imposed on corporations" and still falls within the §742 exception.

In addition to the Montana Corporation License Tax constituting the type of tax contained within the exception

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4. *See*, Respondent's initial Protest to the Department specifically incorporated as Exhibit "C" via item 13 of the Complaint which states: "taxpayer admits that generally interest income from United States obligations is taxable for purposes of the Montana Corporation License Tax".

5. *See, e.g.*, Respondent's Reply Brief to Montana Supreme Court, p. 2; Reply Brief to Montana District Court, p. 3, both reproduced in Appendix, pp. 51a-52a.

to 31 U.S.C. §742, it also meets the second requirement in that it is nondiscriminatory. As has been already noted, a second issue presented to the Montana Supreme Court in this matter was whether the Montana corporation license tax is discriminatory. Although the Montana court determined this second issue to be moot in light of its decision on the first issue, the Department successfully prevailed at District Court that the Montana tax is not discriminatory since it includes interest income derived from all obligations issued by the State of Montana or any political subdivision thereof, any sister state, or the United States. This is all that is required by §742 according to *Memphis Bank and Trust Company*, 51 U.S.L.W. at 4105:

> It is clear that under the principles established in our previous cases, the Tennessee bank tax cannot be characterized as nondiscriminatory under §742. Tennessee discriminates in favor of securities issued by Tennessee and its political subdivisions and against federal obligations. The State does so by including in the tax base income from federal obligations while excluding income from otherwise comparable state and local obligations. We conclude, therefore, that the Tennessee bank tax impermissibly discriminates against the Federal Government and those with whom it deals.

Notwithstanding that interest income from all obligations are included in the base of the Montana tax, it was argued by the Respondents that because statutes providing for issuance of certain Montana obligations[6] contain tax exempting language, the result is a discriminatory tax. The District Court affirmed the position of the Department that the Montana Corporation License Tax clearly

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6. §§ 7-7-4607, 7-13-2330, 7-14-4654, 7-15-4307, 7-34-2416, 60-11-1110, 60-11-1210, 67-11-306, and 90-6-125, MCA. See Appendix, pp. 53a-54a, for Complete Text of Statutes.

includes in the measurement of the tax, interest income from all Montana obligations. The basis of the District Court's holding, and the Petitioner's argument is that the statutes' tax exempting language prohibits all forms of state taxation except a franchise tax, since such tax does not tax the income but taxes the corporate privilege. Such rationale is supported by decisions of this Court interpreting §742 prior to the 1959 amendment, and the Montana Supreme Court, as well as other federal excise tax decisions.

B. THE MONTANA SUPREME COURT DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN BUT SHOULD BE SETTLED BY THIS COURT.

The imposition by the State of Montana of a corporation license tax which includes interest income from federal obligations in its measuring base is plainly in accord with 31 U.S.C. §742. It is at this point that a question of uniform interpretation of federal statutes presents itself. This Court has never directly addressed the issue of whether the tax immunity described in the specified statutes (31 U.S.C. §769 and 12 U.S.C. §§1433, 1725(e), 2055, 2079, 2134) is broader than that otherwise provided by 31 U.S.C. §742. *See, Memphis Bank and Trust Company v. Riley C. Garner, supra*, fn. 5. This Petitioner believes that the tax exempting language in §742 provides clear guidance as to the interpretation to be given to the exemption language contained in those statutes. The Montana Supreme Court held otherwise and ruled without stating its reason that the specific federal statutes creating the federal obligations prohibit the inclusion of federal interest in the net income measure of the Montana corporation license tax, notwithstanding the interpretation given to the tax exemption language in §742 by this Court. 654 P.2d at 498.

It must be noted that the specific statutes providing for issuance of certain federal obligations contain language exempting the obligations from state taxation. That language is virtually identical to the exempting language contained in the first sentence of 31 U.S.C. §742, which prior to 1959 comprised the entire statute. Because the language is so similar, the same interpretation of the exempting language given to §742 is applicable to the individual agency statutes. The prohibition on state taxation of federal obligations as contained in §742 does not apply to state franchise taxation. The state tax prohibitions contained in the issuing statutes likewise does not apply to a state franchise tax such as the Montana Corporation License Tax.

Beginning in 1862 this Court interpreted §742 and instituted a long line of decisions upholding the position that states could levy a franchise or excise tax for a granted privilege such as operation in corporate form, and that in computing the value of that privilege consideration of the value of federal obligations held as assets did not violate §742. In short, states could tax the franchise and include the value of interest income from federal obligations in the income measurement. *See, Society for Savings v. Coite*, 6 Wall. 594 (1867); *Provident Institution for Savings v. Massachusetts*, 6 Wall. 611 (1867); *Hamilton Co. v. Massachusetts*, 6 Wall. 632 (1867); *Home Insurance Company v. New York State*, 134 U.S. 594 (1890); *Cleveland Trust v. Landers*, 184 U.S. 111 (1902); *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911); *Educational Films Corporation v. Ward*, 282 U.S. 379 (1931); *Pacific Co. v. Johnson*, 285 U.S. 480 (1932); and *Werner Machine Co. v. Director of Taxation*, 350 U.S. 492 (1956). Succinctly stated, the latest ruling announced in these cases was that a franchise tax does not violate 31 U.S.C. §742 merely because it is measured by a yardstick which includes tax-

exempt income or property, even though a part of the economic impact of the tax may be said to bear directly upon such income or property. *See, Werner Machine Co.*, 350 U.S. at 494.

In 1959 the second sentence was added to 31 U.S.C. §742. As noted in the legislative history, treatises, and by the Montana District Court, although not addressed by the Montana Supreme Court, this second sentence was but a clarification of the exemptive provision contained in the original sentence which expressly ratifies and reinforces the line of decisions announced by this Court interpreting §742. That line of cases specifically allows a state to levy a nondiscriminatory franchise tax which includes federal interest income in its measure.

In none of these cases, however, was the argument directly addressed as to whether the exempting language contained in the individual statutes providing for issuance of federal obligations is broader than the exemption provided for in 31 U.S.C. §742. A need for guidance from this Court is evident since the issue presented by this petition is significant and potentially far reaching. The issue of a state's ability to levy a corporate franchise tax and choose a method of measurement which it considers the most appropriate to the exercise of that corporate franchise, deserves plenary consideration by this Court. This case offers a timely opportunity for the court to set the matter to rest.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Supreme Court of Montana.

Respectfully submitted,

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ALEXANDER L. STEVAS,
CLERK

82-1471

No. _____

In The

Supreme Court of the United States

October Term, 1982

—o—

THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION

Respondents.

—o—

APPENDIX

—o—

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APPENDIX A

No. 81-528

IN THE SUPREME COURT OF THE
STATE OF MONTANA

1982

FIRST FEDERAL SAVINGS & LOAN ASSOCIATION,
A Federally Chartered Association et al.,
Plaintiffs and Appellants,

vs.

DEPARTMENT OF REVENUE et al.,
Defendants and Respondents.

Appeal from: District Court of the First Judicial District,
In and for the County of Lewis and Clark,
Honorable Gordon Bennett, Judge presiding

Counsel of Record:

For Appellants:

Cannon and Sheehy, Helena, Montana
Edmund F. Sheehy Jr. argued, Helena, Montana

For Respondents:

Michael J. Rieley argued, Helena, Montana

Submitted: June 28, 1982
Decided: September 23, 1982

Filed: Sept. 23, 1982

/s/ THOMAS J. KEARNEY
Thomas J. Kearney
Clerk

Honorable Joel G. Roth, District Judge, delivered the Opinion of the Court.

First Federal Savings and Loan Association of Missoula (Missoula First Federal) and Havre Federal Savings and Loan Association (Havre Federal) (hereinafter also referred to as the "taxpayers") appeal from a summary judgment granted to the Department of Revenue (Department) by the District Court of Lewis and Clark County. We reverse.

Missoula First Federal and Havre Federal are federally chartered savings and loan associations doing business in the State of Montana. As such, they are subject to the Montana Corporation License Tax pursuant to the provisions of section 15-31-101(4), MCA. The Department of Revenue is the state agency responsible for the administration and collection of the Montana Corporation License Tax pursuant to section 15-31-111, MCA.

These two taxpayers are required annually to pay to the state treasurer 6¾ percent of their respective net incomes as a license fee for the privilege of carrying on business in Montana. See sections 15-31-121 and 15-31-101(3), MCA. Each of these taxpayers filed its Montana Corporation License Tax return for the calendar tax year of 1979.

In order to arrive at the net income upon which the tax is based, each taxpayer had deducted from its gross income the interest income it had received from its investments in several federal obligations. Additionally, Havre Federal deducted a net operating loss from prior years which was carried over to 1979.

After the Department of Revenue received the tax returns for 1979 and examined same, the Department disallowed the deduction for interest income on federal obligations on each tax return and also disallowed the deduction of the net operating loss carryover on Havre

Federal's return. The Department computed that Missoula First Federal owed an additional license tax of $12,271.00 plus interest and Havre Federal owed an additional license tax of $47,010.78 plus interest. A notice of the disallowances and resulting tax deficiencies was sent to each taxpayer.

Each taxpayer filed a written protest pursuant to section 15-31-503, MCA, with the Department and when the Department refused to reconsider its position, the two taxpayers joined together and filed a declaratory judgment action against the Department on November 12, 1980, in the District Court of Lewis and Clark County, seeking a judicial interpretation of the several state and federal statutes involved plus a judgment declaring part of one state statute relating to the calculation of net operating loss carryovers to be unconstitutional because of its retroactive application.

Because only questions of law were raised by the allegations in the complaint and answer, the taxpayers filed their motion for summary judgment on April 3, 1981. Subsequently, the Department filed its motion for summary judgment. Written memoranda were filed by both sides and oral argument was presented on May 28, 1981. The District Court granted the Department's motion, denied the taxpayers' motion and issued a summary judgment with a memorandum decision on August 19, 1981.

The effect of the District Court's summary judgment was that the interest income from the federal obligations was not deductible from gross income in arriving at taxable net income, that the net operating loss incurred in prior years could not be carried over and deducted in 1979 by Havre Federal and that the state statutory provision relating to net operating loss carryovers did not violate the constitutional prohibition against retroactive application of a state statute. It is from that summary

judgment and the order denying the taxpayer's motion for summary judgment that the taxpayers appeal, raising the following three issues for appellate review:

First Issue: Did the District Corut err by deciding that interest income from certain federal obligations is includable in net income and hence subject to the Montana Corporation License Tax? We hold there was error on this issue.

Second Issue: Did the District Court err in deciding that the Montana Corporation License Tax is not discriminatory? We hold that this issue is moot in view of our decision on the first issue.

Third Issue: Did the District Court err in deciding that section 15-31-114(2)(b)(ii)(C), MCA, is not constitutionally retroactive? We hold there was error on this issue.

FIRST ISSUE

The taxpayers contend the following interest income from the federal obligations indicated is exempt from the Montana Corporation License Tax:

FEDERAL OBLIGATION	INTEREST INCOME
U.S. Treasury Bills	$ 3,843.65
Federal Home Loan Bank Notes	38,120.61
Federal Land Bank Obligations	118,325.70
Federal Farm Credit Bank Securities	4,695.82
Federal Home Loan Bank Dividends on Stocks	48,013.00
Federal Savings and Loan Insurance Corporation—30% of Insurance Premium and Partial Payback	8,475.00

The District Court, in holding that the interest income from the federal obligations was includable in net income

for purposes of calculating the Montana Corporation License Tax, cited and relied on a federal statute, 31 U.S.C. § 742 (1976), which provides as follows:

> "Except as otherwise provided by law, all stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations and except estate taxes or inheritance taxes."

The District Court reasoned that the exception stated in the above federal statute applied to the Montana Corporation License Tax, which is admitted by the parties herein to be a franchise tax, and hence the interest income from the federal obligations is includable in the net income which is the basis upon which the license tax is computed.

The taxpayers had unsuccessfully contended in the District Court that the specific federal statutes which created the federal obligations and authorized their issuance expressly exempted both the principal and the interest paid thereon from all state taxation except estate and gift taxes. The federal statutes which created the federal obligations involved herein, authorized their issuance and contain the exemption are 12 U.S.C. § 1433 (1976), 12 U.S.C. § 1725(e) (1976), 12 U.S.C. § 2055 (1976), 12 U.S.C. § 2079 (1976), 12 U.S.C. § 2134 (1976) and 31 U.S.C. § 769 (1976). Those federal statutes expressly provide that the principal and interest of the various federal obligations are exempt from all state taxation except certain taxes not relevant herein.

The Department argued that the Montana Corporation License Tax is a franchise tax on the *privilege* of doing

business in Montana with the tax based upon or measured by the net income of the taxpayer. Hence, it was argued, that the tax is not on the property (interest income) but is on the privilege. This Court finds the argument to be unpersuasive. It is a distinction without a difference in our opinion. If the franchise tax is on the privilege and the tax is based on the net income, this Court concludes that the tax is on the privilege *and* the net income. If the net income includes tax-exempt interest, the tax is on exempt income which is prohibited by the specific federal statutes creating the federal obligations and granting the tax exemption. The Montana Supreme Court held in 1976 in the case of Security Bank v. Connors and Colbo (1976), 170 Mont. 59, 550 P.2d 1313, that the Montana Corporation License Tax is a tax on net income. It also appears to this Court that by the Department's including the tax-exempt interest in net income, the Department is seeking to tax indirectly what it cannot tax directly, in violation of the general rule set forth in 31 U.S.C. § 742 (1976). See, Federal Products Corp. v. Norberg (R.I. 1981), 429 A.2d 447.

In the *Federal Products Corp.* case, a Rhode Island industrial corporation had invested cash in federal obligations which were exempt from state taxes. The corporation was subject to the Rhode Island Business Corporation Tax, which was not a franchise tax but rather was a tax on the net income of the corporation. The corporation had deducted the interest income from its gross receipts in arriving at the net income subject to the state tax. The tax administrator refused to allow the deduction and included the interest income in the corporation's taxable net income. The lower court affirmed the tax administrator but, on appeal to the Rhode Island Supreme Court, the interest income from the federal obligations was held to be exempt from the state tax. The decision emphasizes that the tax

administrator was attempting to do *indirectly* what he could not do directly, i.e., levy a state tax on interest income from federal obligations when the federal obligations and the interest therefrom were expressly declared to be exempt from state taxation pursuant to 31 U.S.C. § 742 (1976). The Rhode Island Supreme Court said that although the tax administrator contended that he included the interest income merely as a measure to determine the corporate income tax due to the state, he overlooked the fact that the amount of the tax assessed was increased by more than $11,000.00 by the inclusion of the tax-exempt interest from the tax-exempt federal obligations in the measure of the tax. That court concluded by saying that the only conclusion to draw is that the state tax was an *indirect* tax on exempt federal obligations and their interest and hence invalid.

During oral argument on this appeal, the taxpayers' counsel orally cited the recent Tennessee case of Memphis Bank and Trust Co. v. Garner (Tenn. 1981), 624 S.W.2d 551, as a case found after the briefs on appeal were filed. That case is contrary to the taxpayers' position herein. That case involved a local bank excise tax which was computed on the bank's net earnings which included interest from tax-exempt federal obligations. The Tennessee Supreme Court said there was nothing in the general federal exemption statute (31 U.S.C. § 742 (1976)) or in the particular federal exemption statutes pertaining to the federal obligations involved that prohibited the state from measuring the bank excise tax on net earnings which included interest on federal obligations. Counsel stated that the case has been appealed to the United States Supreme Court and certiorari has been granted. We disagree with the Tennessee court. It is our opinion that both the general federal exemption statute and the individual particular federal exemption statutes clearly exempt the interest

income of the federal obligations involved in the instant case from the Montana Corporation License Tax.

In summary on the first issue, we hold that the District Court erred and that the interest income received by the taxpayers on the exempt federal obligations is not includable in net income for the purpose of calculating the Montana Corporation License Tax.

SECOND ISSUE

Since we decided that the interest income from the tax-exempt federal obligations involved herein is not includable in net income for the purpose of computing the Montana Corporation License Tax, the second issue becomes moot.

THIRD ISSUE

The District Court held there was no unconstitutional retroactive application of section 15-31-114(2)(b)(ii)(C), MCA, to Havre Federal's 1979 tax return. Havre Federal had incurred a net operating loss in each of the five years from 1974 through 1978. Those losses occurred because, prior to 1979, interest income from federal obligations was not subject to the Montana Corporation License Tax because interest income from state obligations was specifically exempt from said tax. Hence, when Havre Federal deducted the federal interest income from gross income in arriving at net income on its tax returns for those earlier years, a net operating loss resulted.

Section 15-31-114(2)(b)(i), MCA, provides for the carrying forward of net operating losses. Under that statute Havre Federal carried forward its net operating losses from 1974 through 1978 and applied same to its 1979 return which resulted in no net income for 1979. It is to be noted that Havre Federal computed its net operating losses in 1974 through 1978 pursuant to the Montana Corporation License Tax statutes *then in effect.*

Section 15-31-114(2)(b)(ii)(C), MCA, provides:

> "Any net operating loss carried over to any taxable years beginning after December 31, 1978, must be calculated under the provisions of this section effective for the taxable year for which the return claiming the net operating loss carryover is filed."

The Department, acting under the authority of the above-quoted statute, recalculated the net income of Havre Federal for the years 1974 through 1978 based upon the 1979 law, which resulted in the adding back of the deducted federal interest income in each of the earlier years which further resulted in the elimination of the net operating losses for each of the earlier years. Hence, there were no operating losses to carry forward to 1979.

It seems clear to this Court that the retroactive application of a 1979 law to the years 1974 through 1978 is unconstitutional. Havre Federal made investment decisions and financial plans based on the tax laws in effect in the years involved. The state cannot change a law in 1979 and compel a recalculation of tax returns filed for 1974 through 1978 based upon the new law effective for the first time in 1979.

This Court stated in the case of Castles v. State ex rel. Department of Highways (1980), ____Mont.____, 609 P.2d 1223, 1225, 37 St.Rep. 734, 736:

> "A retroactive law is one that takes away or impairs vested rights acquired under existing laws or creates new obligations or imposes new duties in respect to transactions already past."

We conclude that section 15-31-114(2)(b)(ii)(C), MCA, is unconstitutional because it requires retroactive application, it is in violation of the due process clause of the federal and state constitutions, and it imposes a new duty on Havre Federal.

CONCLUSION

We reverse the District Court's order denying the taxpayers' motion for summary judgment and reverse the District Court's order granting the Department's motion for summary judgment and remand this case to the District Court for the purpose of entering new orders and summary judgment in conformance with this decision.

/s/ JOEL G. ROTH
Honorable Joel G. Roth, District Judge,
sitting in place of Mr. Justice Fred J. Weber

We concur:

/s/ FRANK I. HASWELL
Chief Justice

/s/ GENE B. DALY
/s/ JOHN CONWAY HARRISON
/s/ DANIEL J. SHEA
/s/ FRANK B. MORRISON, JR.
Justices

/s/ W. W. LESSLEY
Honorable W. W. Lessley, District Judge,
sitting in place of Mr. Justice John C. Sheehy

IN THE SUPREME COURT OF THE
STATE OF MONTANA

No. 81-528

FIRST FEDERAL SAVINGS & LOAN ASSOCIATION
OF MISSOULA, a Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS & LOAN ASSOCIATION,
a Federally Chartered Association,
Plaintiffs and Appellants,

v.

DEPARTMENT OF REVENUE, State of Montana,
Defendant and Respondent.

ORDER

PER CURIAM:

The petition for rehearing is denied.

DATED this 6th day of December, 1982.

/s/ FRANK I. HASWELL
Chief Justice

/s/ GENE B. DALY
/s/ FRANK B. MORRISON, JR.
Justices

/s/ JOEL G. ROTH
Honorable Joel G. Roth, District Judge,
sitting in place of Mr. Justice Fred J. Weber

/s/ W. W. LESSLEY
Honorable W. W. Lessley, District Judge,
sitting in place of Mr. Justice John C. Sheehy

Mr. Justice John Conway Harrison and Mr. Justice Daniel J. Shea would grant a rehearing.

Filed: December 6, 1982

/s/ THOMAS J. KEARNEY
Clerk of Supreme Court
State of Montana

Filed: December 8, 1982

/s/ MARY G. HARRIS

APPENDIX B

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF MONTANA, IN AND FOR THE COUNTY OF LEWIS & CLARK.

FIRST FEDERAL SAVINGS & LOAN OF MISSOULA ASSOCIATION, A Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS & LOAN ASSOCIATION, a Federally Chartered Association,
Plaintiffs,

vs.

DEPARTMENT OF REVENUE OF THE STATE OF MONTANA, an Administrative Agency within the Executive Branch of State Government,
Defendant.

No. 45982

MEMORANDUM AND ORDER

Filed: August 19

Nancy Jones

The complaint in this action was filed November 12, 1980. Defendant answered January 5, 1981. April 3rd the plaintiffs filed a motion for summary judgment. The defendant filed a cross motion for summary judgment May 15th. The matter was argued and briefed and is submitted for decision. There are no disputed facts.

Plaintiffs are taxpayers and are subject to the Montana corporation license tax provided for in Title 15 Chapter 31, MCA. The Department of Revenue is the Department responsible for administration and collection of the tax. In their tax returns for 1979, both plaintiffs deducted interest

income from certain federal obligations from gross income to arrive at net income. In the same returns, plaintiff Havre Federal Savings & Loan applied carryovers from net operating losses incurred in prior years; it carried these amounts over to 1979 without using the method of calculating net operating losses effective for the tax year in question in accordance with Section 15-31-114(2)(ii)(c) MCA (as amended in 1979). The Department disallowed the interest income deductions of both plaintiffs and the net operating loss deduction of Havre Federal Savings & Loan. Missoula First Federal Savings & Loan received a notice of tax deficiency for $12,271.00 plus interest of $108.93 for the 1979 tax year. Havre Federal Savings & Loan received a notice of tax deficiency of $47,010.78 plus interest of $1,135.98 for the 1979 tax year. Both plaintiffs filed written protests with the Department and instituted this action.

The issues presented are as follows:

I. Whether interest income from certain federal obligations, listed in Exhibit A, are includable in the computation of corporation license tax.

II. Whether the Montana corporation license tax is discriminatory.

III. Whether Section 15-31-114(2)(ii)(c) is unconstitutionally retroactive.

I.

Interest income from federal securities which are tax-exempt under those specific statutes listed in Exhibit A are includable in the computation of the Montana corporation license tax. 31 USCA §742 reads:

> All stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require

> that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, *except nondiscriminatory franchise or other non-property taxes in lieu thereof imposed on corporations* and except estate taxes or inheritances taxes. (emphasis added)

Plaintiffs assert the tax-exempt obligations in Exhibit A are not affected by the above statute, and thus their interest income cannot be included in the computation of corporation license tax under Sections 15-31-101 et seq., MCA. They contend the federal statute applies only to obligations which are not specifically exempted from taxation, as the obligations in Exhibit A are; in other words, the express exemption from taxation of these obligations excludes them from coverage of §742. The issue then is statutory construction and determination of legislative intent.

The first sentence of §742 has been in existence since 1862. The second sentence was added in 1959. Thus before 1959 the federal statute did not expressly exclude franchise taxes from the general tax immunity granted federal obligations and securities. However, despite lack of express provision by statute, the United States Supreme Court traditionally and consistently held that interest and income from tax exempt securities and obligations may be included in computation of franchise and excise taxes without violating constitutional or statutory prohibitions against their taxation. In so holding, the Court held, in effect, that use of the tax exempt securities and obligations as a measurement for franchise and excise taxes is not a "tax" on the securities and obligations, rather it is a tax on the corporate franchise, with reference being made to the obligations, for the sole purpose of determining the amount of tax to be exacted each year. Any inclusion of tax exempt property is "incidental" and not the focus of

the tax. *Home Ins. Co. of New York v. People of the State of New York*, 33 L. Ed. 1025 (1889); *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1910); *Pacific Co. v. Johnson*, 285 U.S. 480 (1932); *Tradesmen's National Bank v. Okla. Tax Commission*, 309 U.S. 560 (1939). In *Northwestern Mutual Life Ins. Co. v. Wisconsin*, 275 U.S. 136 (1927), the Court made a distinction between a franchise tax and a property tax based upon the difference between taxation on gross income, in which event the tax would be deemed to be directly on the income of the federal obligation, and taxation on the net income, in which event the tax would be deemed a measuring device for determination of the franchise tax. In *Macallen Co. v. Massachusetts*, 279 U.S. 620 (1929), the Court, while recognizing that excise taxes generally could be measured by tax exempt securities, emphasized that inclusion of tax exempt property is legitimate as long as "the thing taxed in form was in fact and reality the subject aimed at," and struck down a Massachusetts tax statute declaring that the taxation policies embodied in that state's statutes clearly intended the tax to be for the very purpose of subjecting the tax-exempt securities to the burden of the tax from which they were immune. The Montana Supreme Court in *Montana Bank v. Casey*, 135 Mont. 104, 337 P2d 935 (1959), noted the authority of the legislature to include interest on federal obligations in the corporation's net income in computing the license tax.

When Congress amended §742 in 1959, it intended to clarify, and not to change, the existing law, in two respects: (1) That the tax immunity include indirect as well as direct taxation (see *Montana Bankers' Association v. Montana Department of Revenue*, 117 Mont. 112, 580 P2d 909 (1978); and (2) the immunity does not include

nondiscriminatory franchise and other nonproperty taxes.[1]

To address the individual exemption statutes in Exhibit A, we first note that there are no cases which declare any of these as being outside the scope of 31 USCA §742.

12 USCA §1433 was enacted in 1932 and amended in 1935. It states in pertinent part:

> Any and all notes, debentures, bonds and other such obligations issued by any bank, and consolidated Federal Home Loan Bank bonds and debentures, shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The bank, including its franchise, its capital, reserves, and surplus, its advances, and its income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority;

12 USCA §1725(e) was enacted in 1934. It states in pertinent part:

> (e) All notes, bonds, debentures, or other such obligations issued by the Corporation shall be exempt, both as to principal and interest, from all taxation (except surtaxes,

---

[1] See 1959 U.S. Code Congressional and Administrative News, wherein the analysis of the amendment to 31 USCA §742, the Senate report stated, on p. 2777:

"Under the amendment, a new sentence is added to section 3701. The new sentence makes it clear that the exemption now provided by section 3701 extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporation taxes and except estate taxes or inheritance taxes."

> estate, inheritance, and gift taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The Corporation, including its franchise, capital, reserves, surplus, and income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority;

31 USCA §769 was enacted in 1910. It exempted obligations (issued after 1910) from federal and state taxation. This statute was partially repealed by 31 USCA §742(a), in 1941, which made federal obligations issued after 1941 subject to federal taxation.

§742 as amended in 1959 must be interpreted to govern the securities and obligations whose immunities are created by the above, pre 1959, statutes. It expressly refers to *all* stocks, bonds, treasury notes, and other obligations of the United States. The plain and obvious meaning of the language of a statute must be used, if possible, to determine legislative intent. *National Forest Preservation Group v. Volpe*, 352 F.Supp 123, motion den. 359 F.Supp 136 (D.C. Mont. 1972). Congress is presumed to be cognizant of its earlier enactments. *Texaco, Inc., v. Fed. Power Comm'n.*, 317 F2d 796 (C.A. Okla, 1963) cert. den. 377 U.S. 922; *U.S. v. Hawkins*, 228 F2d 517 (C.A. Alaska 1956).

12 USCA Sections 2055, 2079 and 2134 were all enacted in 1971. 12 USCA §2055, provides:

> Every Federal land bank and every Federal land bank association and the capital, reserves, and surplus thereof, and the income derived therefrom shall be exempt from Federal, State, municipal, and local taxation, except taxes on real estate held by a Federal land bank or a Federal land bank association to the same extent, according to its

value, as other similar property held by other persons is taxed. The mortgages held by the Federal land banks and the notes, bonds, debentures, and other obligations issued by the banks or associations shall be deemed and held to be instrumentalities of the Government of the United States and, as such, they and the income therefrom shall be exempt from all Federal, State, municipal, and local taxation, other than Federal income tax liability of the holder thereof under the Public Debt act of 1941 (section 742(a)[1] of Title 31).

12 USCA §2079, provides:

Every Federal intermediate credit bank and the capital, reserves, and surplus thereof and the income derived therefrom shall be exempt from Federal, State, municipal, and local taxation except taxes on real estate held by a Federal intermediate credit bank to the same extent, according to its value, as other similar property held by other persons is taxed. The obligations held by the Federal intermediate credit banks and the notes, bonds, debentures, and other obligations issued by the banks shall be deemed to be instrumentalities of the Government of the United States, and, as such, they and the income therefrom shall be exempt from all Federal, State, municipal, and local taxation, other than Federal income tax liability of the holder thereof under the Public Debt Act of 1941 (section 742(a)[1] of Title 31).

12 USCA §2134, provides:

Each bank for cooperatives and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such bank shall be exempt, both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority. Such banks, their property, their franchises, capital, reserves, surplus, and other funds, and their income shall be exempt from all taxation now or hereafter imposed by the United

States or by any State, territorial, or local taxing authority; except that interest on the obligations of such banks shall be subject only to Federal income taxation in the hands of the holder thereof pursuant to the Public Debt Act of 1941 (section 742(a)[1] of Title 31) and except that any real and tangible personal property of such banks shall be subject to Federal, State, territorial, and local taxation to the same extent as similar property is taxed.

None of these sections expressly or impliedly contradict or repeal §742 as amended in 1959. Nor do they depart particularly from the language used in tax statutes which have been judicially interpreted not to preclude use of tax exempt obligations and securities in franchise taxes. Again, when Congress enacted these 1971 statutes it is presumed to have known its prior enactments and the judicial interpretations thereof. To support this proposition in fact, we note the House report's analysis of §2055: "The existing law relating to the tax status of land banks and associations is reenacted by this section . . . ." 1971 *U.S. Code Congressional and Administrative News*, 2107.

As to §2079, the same report stated on page 2109: "The tax status of the Federal intermediate credit banks is stated separately in this section and is identical in substance with the present law." As to §2134, it stated on page 2113: "The tax status of the banks for cooperatives under existing law is reenacted." The existing laws referred to did not differ from or contradict 12 USCA §742 or existing judicial interpretation of the tax law in regard to franchise taxes.

For the above reasons we conclude the legislature is not prohibited from including interest income from the obligations listed in Exhibit A in determining corporation license taxes.

II.

The Montana corporation license tax is not discriminatory. Plaintiffs contend it is because the statutes do not permit the Department to include interest income from state obligations in its computation while interest income from federal obligations can be included.

Section 15-31-112 provides: "The license fee shall be computed on the basis of the corporation's total net income for the taxable period." The net income is the gross income minus specified deductions. "Gross income" means "all income recognized in determining the corporation's gross income for federal income tax purposes but shall include interest exempt from federal income tax." 15-31-113(1). This language clearly permits the inclusion of all interest income in the computation of gross income. The plaintiffs assert that the specific state obligations listed in the attached Exhibit B expressly exempt these obligations from any taxation, including the license tax. The tax exemption provisions in the statutes listed in Exhibit B are all substantially the same. For example: 90-6-125 provides that the obligations, their transfer and income ". . . shall be free from taxation by the state. . . ." Other statutes declare that the obligations are "exempt" or "free" from all state taxation.

We first note there is no case law interpreting any of the statutes listed in Exhibit B with respect to their immunity from corporation license tax. The Montana Supreme Court has never had occasion to interpret any of Montana's tax exemption statutes to preclude the use of those obligations in the computation of license or excise taxes. It has, as previously noted, recognized the federal interpretation of federal tax law to permit the use of tax exempt obligations in computing franchise taxes. *Montana Bank v. Casey*, supra. The term "exempt from taxation"

has acquired, through decades of judicial interpretation a peculiar legal meaning; according to that meaning tax-exempt obligations and securities can be used as a measure for computation of franchise taxes. Because neither Montana's legislature not its Supreme Court has expressed anything to the contrary with respect to tax immunity of state obligations, this Court is obliged to apply the same construction to the statutes presently in issue. 1-2-106 MCA; *State Dept. of Highways v. Public Employees Craft Council of Mont.*, 165 Mont. 349, 529 P2d 785. We therefore conclude that the state obligations in the statutes listed in Exhibit B are includable in the computation of gross income for corporation license tax under Section 15-31-113 MCA.

III.

Section 15-31-114(2)(ii)(C) is not unconstitutionally retroactive. That subsection reads:

> "Any net operating loss carried over to any taxable years beginning after December 31, 1978, must be calculated under the provisions of this section effective for the taxable year for which the return claiming the net operating loss carryover is filed."

Before December 31, 1978, interest income from state and federal obligations were deducted from the corporation's gross income for computation of license tax. State law was amended in 1979 to allow inclusion of interest income from state and federal obligations in net income for the purpose of calculating the corporation license tax. The corporation's net income is thus greater if computed under the 1979 law than under prior law. In order to apply 15-31-114(2)(ii)(C) to the corporation's losses carried over from prior years, the Department had to recompute the net income from the prior years according to the 1979 law: the once exempt obligations had to be added back into net income. After recomputing the income for those

prior years, the Department found that there were no losses to be carried over into 1979, and therefore disallowed the loss carryover deduction claimed by the plaintiff for 1979. The Department assessed deficiencies for 1979, but not for the previous years.

It is within the constitutional power of the legislature to enact or amend statutes to apply retroactively as long as they do not impair obligations of contract or disturb vested rights. The legislature may change the mode of collecting taxes which have already been assessed at any time before they have been paid or otherwise discharged. There is no vested right in a mode of procedure for collecting taxes. *O'Brien v. Ross*, 144 Mont. 115, 393 P2d 1013 (1964); *Snow's Mobile Homes, Inc. v. Morgan*, Wash. 494 P2d 216 (1972). No person has a vested right to have a law unchanged for his benefit. *Lines v. City of Topeka*, Kan. 577 P2d 412 (1978); *Seattle First Nat. Bank v. Shoreline Concrete Co.*, Wash. 588 P2d 1308 (1978). A taxpayer has no vested right to have his current taxes computed on the same basis as prior taxes have been. *Filoli, Inc., v. Johnson*, Cal. 51 P2d 1093 (1935). The computation of a franchise tax for a given year can be measured by transactions and income of prior years. *State v. J. C. Maguire Construction Co.*, 113 Mont. 324, 125 P2d 433 (1942); *Filoli, Inc. v. Johnson*, supra; *Title Ins. & Trust Co. v. Franchise Tax Bd.* Cal. 302 P2d 79 (1956). It is the general rule, and not an exception, with regard to availability of loss carryback and carryover, that the loss is treated as though it occurred in the year to which it is to be carried. *Christian v. Dept. of Rev.*, Or. 526 P2d 538 (1974), and cases cited therein. Thus, so long as the recalculation of prior years' net income is not used to retax the corporation for those previous years, that is to say, the new computation is applied prospectively, the tax is not unconstitutional.

Plaintiffs argue that they accrued a vested right at the time their losses were incurred, that right being the use of the existing statute allowing them to carry over their net losses for seven years. The net losses were required to be carried back one year at a time for three years, then carried forward one year at a time for seven years until the losses were used up. Each year to which the loss was applied could use only enough of the loss until the net income for that year equalled zero. (ARM 42.23.411 et seq., provides a more understandable explanation of this procedure than the language in Section 15-31-114 MCA). Thus in order to take advantage of the loss carryback and carryover in any given year, the corporation must have a net profit for that year. It is thus apparent that the use of loss carryback and carryover for losses incurred in a given year is *contingent* upon the corporation's future income. A right is not vested if it is qualified by contingencies. *Robert v. Ellis*, Or. 368 P2d 342 (1962); *State v. Estes Corp.*, Ariz. 558 P2d 714 (1976); *Christian v. County of Ontario*, N.Y. 399 NYS2d 379 (1977).

We therefore conclude Section 15-31-114(2)(ii)(C) is not unconstitutionally retroactive on its face or in its application to plaintiffs.

Plaintiffs' motion for summary judgment is DENIED; defendant's cross-motion for summary judgment is GRANTED.

Dated this 19th day of August, 1981.

GORDON R. BENNETT
District Judge

cc to:

Cannon Law Office
2031 Eleventh Avenue, Helena, Mt.,

Dept. of Revenue, Legal Division
Mitchell Building, Helena, Mt.,

EXHIBIT A

Security	Interest Earned	Statute Conferring Tax Exempt Status
U.S. Treasury Bills	$3,843.65	31 U.S.C. Section 769
Federal Home Loan Bank Notes	$38,120.61	12 U.S.C. section 1433
Federal Land Bank Obligations	$118,325.70	12 U.S.C. section 2055
Federal Farm Credit Bank Security	$4,695.82	12 U.S.C. sections 2079 and 2134
Federal Home Loan Bank Dividends on Stock	$48,013.00	12 U.S.C. section 2134
Federal Savings and Loan Insurance Corporation 30% of Insurance Premium and Partial Payback	$8,475.00	12 U.S.C. section 1725(e)

EXHIBIT B

a. Board of Housing Bonds (Section 90-6-125, MCA);

b. Municipal Refunding Revenue Bonds (Section 7-7-4605, MCA);

c. Airport Authority Revenue Bonds (Section 67-11-303, MCA);

d. Railroad and Rehabilitation Bonds (Section 60-11-1109, MCA);

e. Railroad Rolling Stock Revenue Bonds (Section 60-11-1203, MCA);

f. Urban Renewal Bonds (Section 7-15-4302, MCA);

g. County Water and Sewer District Bonds (Section 7-13-2329, MCA);

h. Municipal Parking Commission Revenue Bonds (Section 7-14-4646, MCA);

i. Bonds for Financing County Hospitals and Nursing Homes (Section 7-34-2411, MCA).

3. That the matters and things set forth above are true and correct to the best of his knowledge and belief.

FURTHER AFFIANT SAYETH NOT.

DEPARTMENT OF REVENUE
Corporation Tax Division
Mitchell Building
Helena, Montana 59620

/s/ GERALD L. FOSTER
Gerald L. Foster
Administrator

State of Montana)
County of Lewis and Clark) ss.

On this 13th day of May, 1981, before me a Notary Public for the State of Montana, personally appeared

Gerald L. Foster known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same in his capacity as Administrator of the Corporation Tax Division of the Department of Revenue of the State of Montana and also in his capacity as a private individual.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my Official Seal the day and year in this certificate above written.

/s/Raini Williams
NOTARY PUBLIC for the
State of Montana
Residing at Clancy
My Commission Expires:
October 30, 1983

(SEAL)

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF MONTANA, IN AND FOR THE COUNTY OF LEWIS AND CLARK

No. 45982

FIRST FEDERAL SAVINGS & LOAN OF MISSOULA ASSOCIATION, a Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS & LOAN ASSOCIATION, a Federally Chartered Association,
Plaintiffs,

vs

DEPARTMENT OF REVENUE OF THE STATE OF MONTANA, an Administrative Agency within the Executive Branch of State Government,
Defendant.

NOTICE OF ENTRY OF JUDGMENT

TO: Edmund F. Sheehy, Jr.
Cannon, Parrish and Sheehy
2031 Eleventh Avenue
Helena, Montana 59601

PLEASE TAKE NOTICE pursuant to Rule 77(d), Montana Rules of Civil Procedure, that the enclosed document is a true copy of the Order of the Court and Memorandum entered in the above-captioned matter on the 19th day of August, 1981.

DATED this 25 day of August, 1981.

CLARA GILREATH,
Clerk of District Court

Filed: Aug. 25, 1981

/s/ Hilda Funk
Deputy Clerk

APPENDIX C

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF MONTANA, IN AND FOR THE COUNTY OF LEWIS AND CLARK

Cause No. 45982

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, A Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION, A Federally Chartered Association,
Plaintiffs,

v

DEPARTMENT OF REVENUE, State of Montana, an administrative agency within the Executive Branch of state government,
Defendant.

ORDER AND JUDGMENT

Filed: Dec. 20, 1982

Mary Root

On September 23, 1982, the Montana Supreme Court reversed this Court's memorandum and order of August 19, 1981, granting summary judgment to the Department of Revenue herein and the Supreme Court directed that a new order and summary judgment be entered in this cause, in accordance with the opinion of the Montana Supreme Court. Thereafter, the Court on December 6, 1982, denied the Department of Revenue's petition for rehearing and remittitur was issued to this Court.

NOW THEREFORE, based on the Opinion of the Montana Supreme Court;

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that:

1. Plaintiffs' motion for summary judgment is hereby granted and the Department's cross-motion for summary judgment is denied;

2. That the interest income from the federal obligations held by plaintiffs, which are: Federal Home Loan Bank Notes, Federal Land Bank Obligations, Federal Farm Credit Securities, Federal Home Loan Bank dividends on stock held by plaintiffs, Federal Savings and Loan Insurance Corporation obligations, and U.S. Treasury Bills are hereby declared to be exempt from taxation for purposes of the Montana Corporation License Tax because the federal statutes involved herein: 12 U.S.C. sections 1433, 2055, 2079, 2134, 1725(e) and 31 U.S.C. section 769 expressly provide that the interest income from these particular obligations is exempt from any form of state taxation which would and does include the Montana Corporation License Tax;

3. That the amendment to section 15-31-114(2)(b)(ii)(C), MCA, concerning the method of calculating net operating loss carry-over from prior years, is declared to be unconstitutional and void as violative of the due process clause of the both the United States Constitution and the Montana Constitution;

4. That defendant is hereby ordered to refund the illegal taxes collected in the sum of $12,379.93 to First Federal Savings and Loan Association of Missoula, who paid this amount under protest prior to the institution of this lawsuit and the sum of $48,146.76 to Havre Federal Savings and Loan Association, who paid this amount under protest prior to the institution of this lawsuit; and

5. That plaintiffs recover their costs incurred in this litigation.

DATED this 16th day of December, 1982.

GORDON R. BENNETT
District Judge

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF MONTANA, IN AND FOR THE COUNTY OF LEWIS AND CLARK

Cause No. 45982

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, A Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION, A Federally Chartered Association,

Plaintiffs,

v

DEPARTMENT OF REVENUE, State of Montana, an administrative agency within the Executive Branch of state government,
Defendant.

NOTICE OF ENTRY OF JUDGMENT

Please take notice that judgment was entered in the above entitled action in favor of the plaintiffs, a copy of which is attached hereto, on December 16, 1982.

DATED this 20 day of December, 1982.

CLARA GILREATH
Clerk of the District Court
First Judicial District
SEAL Lewis & Clark County, Montana
By /s/ Mary Root

CERTIFICATE OF SERVICE

This is to certify that the attached Notice of Entry of Judment was july served upon all parties of record by mailing a copy thereof, postage prepaid, to them or their attorneys at their addresses set forth below on the 20 day of December, 1982.

/s/ Mary Root

Michael J. Rieley, Esq.
Legal Bureau
Department of Revenue
Mitchell Building
Helena, MT 59620

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF MONTANA, IN AND FOR THE COUNTY OF LEWIS AND CLARK

No. 45982

FIRST FEDERAL SAVINGS & LOAN ASSOCIATION OF MISSOULA, a Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS & LOAN ASSOCIATION, a Federally Chartered Association,
Plaintiffs,

vs

DEPARTMENT OF REVENUE, State of Montana, an administrative agency within the Executive Branch of State Government,
Defendant.

ORDER

Filed: Dec. 30, 1982

/s/ Nancy Jones

This Court, upon Motion of Michael J. Rieley, an attorney for the Respondent, Montana Department of Revenue, having reviewed the authorities relevant thereto does hereby;

ORDER that entry of Final Judgment in this matter and any execution and enforcement thereon are hereby stayed pending application for Appeal or Writ of Certiorari to the Supreme Court of the United States with respect to the federal questions raised herein.

DATED this 29th day of December, 1982.

/s/ Gordon R. Bennett
District Judge

APPENDIX D

31 U.S.C. Section 769, UNITED STATES TREASURY BILLS

§769. Certificates of indebtedness; taxation; expense of issue

Any certificates of indebtedness hereafter issued [after February 4, 1910] shall be exempt from all taxes or duties of the United States (but, in the case of certificates issued after September first, nineteen hundred and seventeen, only if and to the extent provided in connection with the issue thereof), as well as from taxation in any form by or under State, municipal, or local authority; and a sum not exceeding one-tenth of one per centum of the amount of any certificates of indebtedness issued is hereby appropriated, out of any money in the Treasury not otherwise appropriated, to pay the expenses of preparing, advertising, and issuing the same.

12 U.S.C. Section 1433, FEDERAL HOME LOAN BANK NOTES

§1433. Exemption from taxation; obligations acceptable as credit on debt of home owner

Any and all notes, debentures, bonds, and other such obligations issued by any bank, and consolidated Federal Home Loan Bank bonds and debentures, shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The bank, including its franchise, its capital, reserves, and surplus, its advances, and its income shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority; except that [in] any real property of the bank shall be subject to State, Territorial, county, municipal, or local taxation to the

same extent according to its value as other real property is taxed. The notes, debentures, and bonds issued at any bank, with unearned coupons attached, shall be accepted at par by such bank in payment of or as a credit against the obligation of any home-owner debtor of such bank.

12 U.S.C. Section 1725(e), FEDERAL SAVINGS & LOAN INSURANCE CORPORATION NOTES

§1725. Creation of Federal Savings and Loan Insurance Corporation

* * *

(e) Taxation. All notes, bonds, debentures, or other such obligations issued by the Corporation shall be exempt, both as to principal and interest, from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality or local taxing authority. The Corporation, including its franchise, capital, reserves, surplus, and income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority; except that any real property of the Corporation shall be subject to State, territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed.

12 U.S.C. Section 2055, FEDERAL LAND BANK OBLIGATIONS

§2055. Taxation

Every Federal land bank and every Federal land bank association and the capital, reserves, and surplus thereof, and the income derived therefrom shall be exempt from Federal, State, municipal, and local taxation, except taxes on real estate held by a Federal land bank or a Federal land bank association to the same extent, according to its value, as other similar property held by other persons is taxed. The mortgages held by the Federal land banks

and the notes, bonds, debentures, and other obligations issued by the banks or associations shall be deemed and held to be instrumentalities of the Government of the United States and, as such, they and the income therefrom shall be exempt from all Federal, State, municipal, and local taxation, other than Federal income tax liability of the holder thereof under the Public Debt Act of 1941 (31 U.S.C. 742(a)).

12 U.S.C. Section 2079, FEDERAL FARM CREDIT BANK SECURITIES

§2079. Taxation

Every Federal intermediate credit bank and the capital, reserves, and surplus thereof and the income derived therefrom shall be exempt from Federal, State, municipal, and local taxation except taxes on real estate held by a Federal intermediate credit bank to the same extent, according to its value, as other similar property held by other persons is taxed. The obligations held by the Federal intermediate credit banks and the notes, bonds, debentures, and other obligations issued by the banks shall be deemed to be instrumentalities of the Government of the United States, and, as such, they and the income therefrom shall be exempt from all Federal, State, municipal, and local taxation, other than Federal income tax liability of the holder thereof under the Public Debt Act of 1941 (31 U.S.C. 742(a)).

12 U.S.C. Section 2134, FEDERAL HOME LOAN STOCK DIVIDENDS

§2134. Taxation

Each bank for cooperatives and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such bank shall be exempt, both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority. Such

banks, their property, their franchises, capital, reserves, surplus, and other funds, and their income shall be exempt from all taxation now or hereafter imposed by the United States or by any State, territorial, or local taxing authority; except that interest on the obligations of such banks shall be subject only to Federal income taxation in the hands of the holder thereof pursuant to the Public Debt Act of 1941 (31 U.S.C. 742(a)) and except that any real and tangible personal property of such banks shall be subject to Federal, State, territorial, and local taxation to the same extent as similar property is taxed. The exemption provided in the preceding sentence shall apply only for any year or part thereof in which stock in the bank for cooperatives is held by the Governor of the Farm Credit Administration.

IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT IN AND FOR THE STATE OF MONTANA, COUNTY OF LEWIS AND CLARK

Cause No. 45982

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, A Federally Chartered Association,
and
HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION, Federally Chartered Association,
Plaintiffs,

vs

DEPARTMENT OF REVENUE, State of Montana, an administrative agency within the Executive Branch of state government.
Defendants.

COMPLAINT

GORDON R. BENNETT
Presiding Judge

Filed: Nov. 12, 1980

By /s/ Hilda Funk
Clerk of District Court

COMES NOW the plaintiffs and complain of defendant and allege:

1. Plaintiffs, FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA and HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION, are federally chartered savings and loan associations, doing business in the state of Montana.

2. Plaintiffs are subject to the Montana Corporation License Tax as set out in Title 15, Chapter 31, Parts 1 to 7, M.C.A.

3. Defendant, DEPARTMENT OF REVENUE, is the state agency responsible for the collection of the Montana Corporation License Tax.

4. Prior to the tax year beginning on or after December 31, 1978, plaintiffs in computing net income for purposes of the corporation license tax were allowed to deduct interest income from obligations of the state or any political subdivision or municipality of the state from gross income. Section 15-31-114(5), M.C.A. (1978).

5. As a result of this provision of state law, defendant promulgated and adopted a regulation allowing a deduction from gross income in computing net income for the corporation license tax of any interest income from obligations of the United States because federal law required interest income from these obligations to be treated the same as interest income from state obligations.

6. The federal law relied on by defendant in promulgating this regulation is 31 U.S.C. section 742, which provides that interest income on United States obligations is exempt from state taxation except nondiscriminatory franchise taxes. Since state law, until 1979, specifically exempted interest income from state obligations, a tax on interest income from United States obligations would have been discriminatory.

7. In 1979, the forty-sixth legislature of the state of Montana enacted House Bill 150, Chapter 634 of the Laws of Montana 1979. This act repealed the deduction from gross income in computing net income for the corporation license tax of interest income from obligations of the state or any political subdivision or municipality for tax years beginning on or after December 31, 1978.

8. By repealing this deduction, the legislature intended to authorize the inclusion of interest income from United States obligations as a part of gross income for purposes of

the corporation license tax because interest income from obligations of the state or any political subdivision thereof would now be taxable for purposes of the corporation license tax.

9. In enacting House Bill 150, Chapter 634 of the Laws of Montana 1979, the Montana Legislature amended section 15-31-114 (2) (b) (ii) (c), M.C.A., concerning the calculation of any net operating loss carryover to provide that for taxable years beginning after December 31, 1978, such net operating loss carryover from prior tax years must be calculated under the provisions of the Montana corporation license tax in effect for the taxable year for which the return claiming the net operating loss carryover is filed. This means that in computing a net operating loss carryover for tax years beginning after December 31, 1978, interest income from state and United States obligations must be added back to net income for the tax years prior to December 31, 1978 in which a net operating loss deduction was taken in order to determine whether there is any net operating loss then in those years to carryover.

10. In their tax returns for tax year 1979, plaintiffs deducted a part of their interest income from certain federal and/or state obligations from gross income to arrive at net income for purposes of the Montana corporation license tax. A list of the federal obligations held by plaintiff First Federal Savings and Loan Association of Missoula, and the interest income therefrom which it deducted from its gross income on its corporation license tax return for tax year 1979 is attached hereto as "Exibit A".

11. Plaintiffs, if they had a net operating loss from prior tax years, carried that amount over for tax year 1979 without recalculating the net operating loss for prior tax years as required by section 15-31-114 (2) (b) (ii) (c), M.C.A. A list of the amount of net operating loss carried

forward by plaintiff Havre Federal Savings and Loan Association is attached hereto as "Exhibit B".

12. Defendant, on or about June 24, 1980, issued a notice to plaintiff First Federal Savings and Loan Association of Missoula disallowing the deduction for interest income on United States obligations and notifying plaintiff of a resulting tax deficiency on its corporation license tax for tax year 1979 in the amount of $12,271.00 plus interest in the amount of $108.93.

13. Pursuant to section 15-31-503, M.C.A., on or about July 18, 1980, plaintiff First Federal Savings and Loan Association filed a written protest against this deficiency assesment with defendant. A copy of this protest is attached hereto as "Exhibit C".

14. Defendant, on or about August 27, 1980, issued a notice to plaintiff, Havre Federal Savings and Loan Association, disallowing its net operating loss deduction; deduction of interest income on United States obligations and deduction of interest income on Puerto Rico Bonds. Defendant notified this plaintiff of a resulting tax deficiency for tax year 1979 of $47,010.78 plus interest of $1,135.98.

15. Pursuant to section 15-31-503, M.C.A., plaintiff Havre Federal Savings and Loan Association filed a written protest against this deficiency assessment with defendant. A copy of this protest is attached hereto as "Exhibit D".

16. Plaintiffs contend that while 31 U.S.C. Section 742, as a general rule, authorizes the inclusion of interest income from United States obligations in the calculation of net income for purposes of a nondiscriminatory corporation license tax, this federal statute does not repeal, amend, nullify or control the specific federal statues relating to the federal securities listed on "Exhibit A"

wherein it is provided that the interest income from these securities is specifically exempted from any form of state taxation which would include corporation license taxes.

17. The federal statutes pertaining to the federal securities shown on "Exhibit A", being more specific than the general statute regarding state taxation of interest income from obligations of the United States must be, and are, controlling in determining whether the interest income from such securities is taxable.

18. Plaintiffs contend that House Bill 150, Chapter 634, Laws of Montana 1979, as codified in Title 15, Chapter 31, Parts 1 to 7, is a disciminatory franchise tax in that it attempts to tax all interest income received from United States obligations without taxing all interest income received from obligations of the state or any political subdivision thereof and is, therefore, illegal as being in direct violation of 31 U.S.C. section 742.

19. Plaintiffs contend that amendment made to section 15-31-114 (2) (b) (ii) (c), M.C.A., concerning the calculations of net operating losses for prior tax years is unconstitutional in that it amounts to the taking of a vested property right without due process of law and denies plaintiffs equal treatment under the law in violation of the United States Constitution and the 1972 Montana Constitution.

WHEREFORE, plaintiffs pray:

1. For a judgment declaring House Bill 150, Chapter 634, Laws of Montana 1979, now codified in Title 15, Chapter 31, Parts 1 to 7, M.C.A., illegal and void for amounting to a discriminatory franchise tax on the interest income of United States obligations in direct violation of 31 U.S.C. section 742;

2. For a judgment declaring the interest income from the federal securities shown on "Exhibit A" as being

specifically exempt from taxation for purposes of the Montana corporation license tax as set out in Title 15, Chapter 31, Parts 1 to 7, M.C.A.;

3. For a judgment declaring the amendment made to section 15-31-114 (2) (b) (ii) (c), M.C.A., concerning the method of calculating of net operating losses carried over from prior years to be unconstitutional and void;

4. For plaintiffs' costs herein, and,

5. For any other relief this court deems appropriate.

DATED this 12th day of November, 1980.

CANNON & GILLESPIE
2031 Eleventh Avenue
Helena, MT 59601

By /s/ ROSS W. CANNON
Ross W. Cannon

By /s/ EDMUND F. SHEEHY, JR.
Edmund F. Sheehy, Jr.
ATTORNEYS FOR PLAINTIFFS

EXHIBIT A

Security	Interest Earned	Statute Conferring Tax Exempt Status
U.S. Treasury Bills	$3,843.65	31 U.S.C. Section 769
Federal Home Loan Bank Notes	$38,120.61	12 U.S.C. section 1433
Federal Land Bank Obligations	$118,325.70	12 U.S.C. section 2055
Federal Farm Credit Bank Security	$4,695.82	12 U.S.C. sections 2079 and 2134
Federal Home Loan Bank Dividends on Stock	$48,013.00	12 U.S.C. section 2134
Federal Savings and Loan Insurance Corporation 30% of Insurance Premium and Partial Payback	$8,475.00	12 U.S.C. section 1725(e)

EXHIBIT B

HAVRE FEDERAL SAVINGS AND LOAN
Schedule of Montana Net Operating Losses
December 31, 1979

	Taxable Income Before NOL	Loss Carried Forward	Deduction Claimed Preceding yr.
1971	(45,791.97)		—0—
1972	12,157.43		—0—
1973	(35,303.15)		—0—
1974	(278,880.84)	(278,880.84)	—0—
1975	(278,778.76)	(278,778.76)	—0—
1976	(393,570.79)	(393,570.79)	—0—
1977	(451,453.74)	(451,453.74)	—0—
1978	(245,031.02)	(245,031.02)	—0—

NOL Carry Forward	(1,647,715.15)
NOL Used in 1979	418,890.45

EXHIBIT C

BEFORE THE DEPARTMENT OF REVENUE
STATE OF MONTANA

CORPORATION LICENSE TAX DEFICIENCY
NOTICE FOR FIRST FEDERAL SAVINGS AND
LOAN ASSOCIATION OF MISSOULA

PROTEST

COMES NOW, FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA (taxpayer) and pursuant to section 15-31-503, M.C.A., hereby protests the additional corporation license tax of $12,379.93 sought to be imposed against it by the Department of Revenue (Department) in its notice dated June 24, 1980.

The notice from the Department states that taxpayer owes $12,379.93 in taxes because the Department has included $200,205.00 in taxpayer's net income as interest income from United States obligations held by taxpayer. Taxpayer alleges that this $200,205.00 should not be included in its net income because this interest income is not taxable income.

While taxpayer admits that generally interest income from United States obligations is taxable for purposes of the Montana Corporation License Tax, the $200,205.00 in question here is not taxable income for purposes of the corporation license tax because the federal statutes creating and regulating the United States obligations held by taxpayer and in question herein expressly provide that the interest income from such obligations is exempt from any form of state taxation. Taxpayer contends that $200,205.00 in interest income, which the Department of Revenue seeks to tax, is interest income solely from United States obligations which had and have a specific exemp-

tion from state taxation under federal law. Therefore, taxpayer is not liable for any additional corporation license tax on this interest income which is not taxable.

Taxpayer hereby formally requests that the Department of Revenue grant it a hearing on this additional tax proposed to be assesesd and taxpayer's protest to such assessment.

DATED this 17th day of July, 1980.

/s/ PAUL J. CHUMRAU
Paul J. Chumrau
President of First
Federal Savings and Loan
Association of Missoula

EXHIBIT D

September 24, 1980

Mr. Gerald Foster,
Administrator, Corporate Tax Division
Department of Revenue
Mitchell Building
Helena, Montana 59601

Dear Mr. Foster:

RE: Havre Federal Savings and Loan Association — Deficiency Assessment for Tax Year Ending 12/31/79

This letter is written to officially file a written protest by taxpayer, Havre Federal Savings and Loan Association (hereinafter referred to as "Havre Federal") against the proposed additional tax set forth in the letter from the Department of Revenue to Havre Federal dated August 27, 1980, and accompanying documents from Candee B. Crantz. Havre Federal requests an oral hearing and an opportunity to present additional evidence relating to the referenced claimed tax liability. A copy of the letter sent by Candee B. Crantz and the determination of Montana corporate license tax prepared by her are attached hereto as Exhibit "A".

The grounds upon which this protest is based are as follows:

1. The Department of Revenue has disallowed a net operating loss in the amount of $418,890.48. This net operating loss was disallowed because of a change in Section 15-31-114, MCA, which now provides that a net operating loss carried over to 1979 must be calculated under the provisions regarding deductibility in effect for 1979. Havre Federal alleges that the application of this statute to itself is unlawful, unconstitutional and against public policy because:

(a) Havre Federal invested in securities which paid interest that was tax exempt under Montana law. These securities were purchased in reliance on this favorable tax treatment.

(b) The law in effect during the years in which net operating losses, which are now being redetermined, accrued allowed a reduction in taxable income for those taxpayers who had taxable income and a net operating loss for those taxpayers who did not have taxable income.

(c) For those taxpayers who had taxable income in previous years, the deduction stands unchanged by the recent legislation and the benefit of their previous investment in the securities of the type in question remains while those taxpayers who did not have taxable income were originally granted a tax benefit by a net operating loss carry back or carry forward which is now being disallowed.

The legislation as it effects this taxpayer is unlawful, unconstitutional and against public policy in that the taxpayer has relied upon the application of the deduction in making investments in previous years, the legislation is an ex post facto law and retroactively effects the taxability of the taxpayer's income for previous years. Thus, the legislation is an unconstitutional taking of a protected property right without due process of law under the constitutions of the United States and the State of Montana. The legislation as applied denies the taxpayer equal treatment with other taxpayers under the constitutions of the United States and the State of Montana.

For the above reasons the taxpayer respectfully requests that the Department of Revenue reconsider the proposed

assessment to allow the net operating loss to be carried forward as indicated on the taxpayer's return.

HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION

By /s/ EINAR LUND
Einar Lund
President

cc: Einar Lund

EXTRACT FROM REPLY BRIEF OF SAVINGS & LOAN ASSOCIATIONS TO THE SUPREME COURT OF MONTANA, pp. 3-4.

Defendant, in its memorandum in support of its cross-motion for summary judgment, discuss extensively whether the Montana Corporation License Tax is a franchise tax and whether the interest income from federal obligations can be included in the measure of this tax pursuant to 31 U.S.C. section 742. In making this argument, defendant is in no way advancing this litigation since on page 5 of Plaintiffs' memorandum, the following appears:

> "Plaintiffs agree that the Montana corporation license tax is a franchise tax. Plaintiffs further agree that interest income from federal obligations can be subjected to a non-discriminatory state franchise tax when, unlike the federal obligations in question here, there is no specific federal statute exempting the obligation and the income derived therefrom from taxation by the state. It is only where a federal statute specifically exempts the interest income from a particular federal obligation from state taxation that the plaintiff is authorized to deduct the interest income from taxation under the Montana corporation license tax . . ."

The issue here is not whether the Montana corporation license tax is a franchise tax or whether interest income from federal obligations may generally be included in the computation of such a tax; but, whether the interest income from the specific federal obligations at issue here is exempt from taxation by a state franchise tax. Thus both the Department and plaintiffs agree as to the type of tax being imposed and that interest income from federal obligations can generally be included in the measure of the tax.

EXTRACT FROM REPLY BRIEF OF SAVINGS & LOAN ASSOCIATIONS TO THE MONTANA DISTRICT COURT, p.2.

—2—

IV.

REPLY ARGUMENT

THE DISTRICT COURT ERRED IN HOLDING THAT INTEREST INCOME FROM CERTAIN U.S. OBLIGATIONS HELD BY PLAINTIFFS IS INCLUDIBLE IN THE COMPUTATION OF THE MONTANA CORPORATION LICENSE TAX

In their brief, the Department devotes a substantial amount of space to argue that the Montana corporation license tax, section 15-31-101, et seq., MCA., is a franchise tax. The Department asserts that it is raising this argument because plaintiffs have "overlooked this point." In making this argument, the Department has totally misunderstood plaintiffs' position in this appeal and in this lawsuit. Plaintiffs have never contended and are not now contending that the Montana corporation license tax is anything other than a franchise tax. Plaintiffs' position is simply that the interest income from certain U.S. obligations held by plaintiffs is exempt from all state taxation including a franchise tax. See page 6 of the Appellant's Brief.

To argue that this interest income may be included in taxable income for purposes of the Montana corporation license tax, the Department relies upon a number of United States Supreme Court cases. The cases the Department cites in its brief are: *Flint v. Stone Tracy Company*, 220 U.S. 107, 31 S.Ct. 342, 55 L.Ed. 389 (1910); *Educational Films Corporation v. Ward*, 282 U.S. 379, 51 S.Ct. 170, 75 L.Ed. 400 (1931); *Pacific Co. v. Johnson*,

Section 7-7-4607, MONTANA CODE ANNOTATED, MUNICIPAL REFUNDING BONDS:

> **7-7-4607. Exemption from certain taxes for refunding revenue bonds.** The refunding bonds and the income therefrom shall be exempt from taxation except inheritance, estate, and transfer taxes.

Section 7-14-4654, MCA, MUNICIPAL PARKING COMMISSION REVENUE BONDS:

> **7-14-4654. Exemption from certain state taxes.** All such revenue bonds and the interest or income therefrom are exempt from all taxation in this state, other than gift, inheritance, and estate taxes.

Section 7-13-2330, MCA, COUNTY WATER & SEWER DISTRICT BONDS:

> **7-13-2330. Status of bonds — tax exemption.** Any bonds issued by any district organized under the provisions of this part and part 22 are hereby given the same force, value, and use as bonds issued by any municipality and shall be exempt from all taxation within the state of Montana.

Section 7-15-3407, MCA, URBAN RENEWAL BONDS:

7-15-4307. Tax exemption for bonds. Bonds issued under the provisions of this part and part 42 are declared to be issued for an essential public and governmental purpose and, together with interest thereon and income therefrom, shall be exempted from all taxes.

Section 7-34-2416, MCA, HOSPITAL & NURSING HOME BONDS:

> **7-34-2416. Tax-exempt status of bonds.** Bonds issued by a county pursuant to the provisions of 7-34-2411 through 7-34-2418 are declared to be issued for an essential public and governmental purpose by a political subdivision within the meaning of 15-30-111(2)(a).

Section 60-11-1110, MCA, RAILROAD REHABILITATION BONDS:

60-11-1110. Tax exemption. Bonds and refunding bonds, their transfer, and their income (including any profits made on their sale) are free from taxation by the state or any political subdivision or instrumentality of the state, except for inheritance and estate taxes.

Section 60-11-1210, MCA, RAILROAD ROLLING STOCK REVENUE BONDS:

60-11-1210. Tax exemption. Bonds and refunding bonds, their transfer, and their income (including any profits made on their sale) are free from taxation by the state or any political subdivision or instrumentality of the state, except for inheritance and estate taxes.

Section 67-11-306, MCA, AIRPORT AUTHORITY REVENUE BONDS:

67-11-306. Tax exemption. Any property in this state acquired by an authority for airport purposes, pursuant to the provisions of this chapter, and any income derived by the authority from the ownership, operation, or control thereof shall be exempt from taxation to the same extent as other property used for public purpose.

Section 90-6-125, MCA, BOARD OF HOUSING BONDS:

90-6-125. Tax exemption of bonds. Bonds, notes, or other obligations issued by the board under this part or by local housing authorities under Title 7, chapter 15, parts 21, 44 and 45, their transfer, and their income (including any profits made on their sale) shall be free from taxation by the state or any political subdivision or other instrumentality of the state, excepting inheritance, estate, and gift taxes. The board is not required to pay recording or transfer fees or taxes on instruments recorded by it.

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No. 82-1471

In The

Supreme Court of the United States

October Term, 1982

THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATON,

Respondents.

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATON,

Respondents.

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

The respondents, First Federal Savings and Loan Association of Missoula, and Havre Federal Savings and Loan Association, respectfully pray that this Court deny issuance of a writ of certiorari to review the judgement and opinion of the Supreme Court of Montana entered in the above matter.

OPINION BELOW AND JURISDICTION

Respondents agree that the Opinion below is as set forth in the petition and respondents agree with the jurisdictional state-

ment in the petition.

STATUTES INVOLVED

Petitioner has set forth in its petition and the appendix thereto most of the federal statutes and Montana state statutes involved in this matter. However, petitioner has neglected to mention section 15-31-121, of the Montana Code Annotated, which was the statute relied upon by the Montana Supreme Court in rendering its opinion herein.

Montana Code Annotated:

> **15-31-121. Rate of tax-minimum tax.**
> (1) Percentage of net income to be paid under 15-31-101 shall be six and three-quarters percent of all net income for the taxable period. The rate set forth in this part shall be effective for all taxable years ending on or after February 20, 1971. This rate is retroactive to and effective for all taxable years ending on or after February 28, 1971.
>
> (2) Every corporation subject to taxation under this part shall, in any event, pay a minimum tax not less than fifty dollars.

QUESTION PRESENTED FOR REVIEW

Whether the State of Montana can include interest income from certain federal obligations in the net income of respondents and subject this income to taxation by and through the Montana Corporation License Tax imposed by sections 15-31-101 et seq., Montana Code Annotated.

STATEMENT OF THE CASE

Respondents are federally chartered savings and loan associations doing business in the State of Montana. As such, respondents are subject to the Montana Corporation License

Tax set out in Title 15, Chapter 31, Parts 1 through 7, of the Montana Code Annotated. Petitioner is the state agency responsible for collecting the Montana Corporation License Tax.

Prior to the tax year beginning on or after Decembers 31, 1978, respondents, in computing net income for the Montana Corporation License Tax, were allowed to deduct interest income from obligations of state and political subdivisions of the state from gross income. Section 15-31-114(5), Montana Code Annotated (1978). Pursuant to this section, the petitioner adopted a regulation allowing a like deduction for interest income from United States obligations because federal law required that interest income from such obligations be treated the same as interest income from state obligations for purposes of state taxation. In promulgating this regulation, petitioner relied upon 31 U.S.C. § 742.

In 1979, the Montana legislature enacted House Bill 150, Chapter 634, Laws of Montana, 1979. This act repealed the deduction from gross income of interest income from obligations of state and political subdivisions for tax years beginning on or after December 31, 1978. The intent of the legislature was to subject interest income from federal obligations to the Montana Corporation License Tax. With this legislation, interest income from federal obligations and state and local obligations was to be included in gross income for purposes of this tax. In their returns for tax year 1979, respondents deducted interest income from certain federal obligations from their gross income to arrive at net income for purposes of the Montana Corporation License Tax. The obligations as to which respondents deducted interest income were: United States Treasury Bills, Federal Home Loan Bank notes and dividends, Federal Land Bank obligations, Federal Farm Credit Bank securities, Federal Home Loan Bank dividends, and Federal Savings and Loan Insurance Corporation securities. Respondents took these deductions on the basis of the federal statutes authorizing the issuance

of these obligations, each of which specifically provided that the interest income from these obligations is exempt from all state taxation.

On or about June 24, 1980, petitioner issued a deficiency notice to respondent, First Federal Savings and Loan Association of Missoula, disallowing the deduction for interest income on these obligations and assessing a tax deficiency for tax year 1979. Respondent filed a written protest against this deficiency assessment with petitioner. On or about August 27, 1980, petitioner issued a deficiency notice to respondent, Havre Federal Savings and Loan Association, disallowing its deductions of interest income on the United States obligations. This respondent also submitted a written protest against this deficiency notice. Thereafter, respondents filed a declaratory judgement action in the District Court of the First Judicial District of the State of Montana in and for the County of Lewis and Clark, asking the District Court to declare that, while 31 U.S.C. § 742 generally allows taxation of interest income from federal obligations by a nondiscriminatory franchise tax, this statute does not repeal, amend, nullify, or control the specific federal statutes creating the specific federal obligations involved herein and, since those statutes precluded state taxation of interest income from these federal securities, this exemption applied to franchise taxation as well as all other forms of state taxation.

After this litigation was commenced, petitioner and respondents agreed that there were no issues of fact to be presented to the District Court and that the only issues were issues of law. Accordingly, each party moved for summary judgement herein. The District Court granted petitioner's motion for summary judgement and ruled that this interest income from the federal obligations was subject to taxation under the Montana Corporation License Tax.

Respondents then appealed from the order of the District Court to the Montana Supreme Court. The Montana Supreme

Court, after reviewing lengthy briefs submitted by both parties concerning the history and purpose of 31 U.S.C. § 742 and the case law in Montana pertaining to the Montana Corporation License Tax, plus listening to a lengthy oral judgement by counsel for both parties, reversed the District Court and held that interest income received by respondents from the specific federal obligations involved herein was not includable in net income for purposes of the Montana Corporation License Tax and that, on the basis of section 15-31-122, Montana Code Annotated, and the case of Security Bank v. Connors and Colbo, 170 Mont. 59, 550 P.2d 1313 (1976), the Montana Corporation License Tax was imposed both on the privilege of doing business and on the net income of respondents.

Petitioner submitted a petition for rehearing to the Montana Supreme Court requesting that the Court clarify its opinion herein. Several amicus curiae then appeared to argue in favor of this petition for rehearing. The Court, after considering the briefs submitted by petitioner and the amicus curiae as well as respondents' briefs in opposition to the petition for rehearing, denied the petition for rehearing on December 6, 1982. Pursuant to the remittitur of the Montana Supreme Court, the District Cot of the First Judicial District of the County of Lewis and Clark then entered a new order and judgement in this cause declaring that the interest income from these specific federal obligations involved in this litigation was exempt from taxation under the Montana Corporation License Tax. Thereafter, petitioner sought and obtained a stay of execution on this judgement pending its filing of a petition for certiorari with this Court. Petitioner's writ was filed in March of 1983.

Between the time that petitioner obtained its stay of the final judgement of the District Court and its filing of the petition for writ of certiorari with this Court, the Montana legislature enacted Senate Bill No. 335 of the 48th Legislative Session of the State of Montana, which was specifically designed to address the opinion of the Montana Supreme Court herein and the judgement of the District Court entered in accordance

therewith. This bill became law in April of 1983, with an immediate effective date, and was to apply retroactively to tax years beginning on or after December 31, 1978. This bill is set forth in the appendix hereto as pages 1 through 5.

ARGUMENTS FOR DENYING A WRIT OF CERTIORARI

A. PASSAGE OF SENATE BILL NO. 335 HAS MADE THIS PETITION FOR CERTIORARI AND THE ISSUES INVOLVED HEREIN MOOT.

The issue presented and argued by respondent in this litigation was whether the interest income from the specific federal obligations involved herein was subject to taxation under the Montana Corporation License Tax. Respondents' contention was that this tax, as a franchise tax, could not reach the interest income from these specific federal obligation since the federal statutes authorizing their issuance specifically provided that interest income from these obligations was exempt from all state taxation. The Montana Supreme Court agreed with the position of respondents and held that the interest income from these obligations could not be included in net income for purposes of the Montana Corporation License Tax. When petitioner's petition for rehearing to the Montana Supreme Court was denied, the Montana legislature, through its Revenue Oversight Committee began looking at new methods of taxing financial institutions such as respondents here. One of the methods was set forth in Senate Bill No. 335 of the 48th Legislature of the State of Montana, which has now become law.

Essentially, this bill disallows any deduction of interest income from tax exempt federal obligations for purposes of the Montana Corporation License Tax. The bill also extends the disallowance of this deduction retroactively to all taxable periods during which such income was excluded from gross income. This means that, while respondents may obtain refunds of the taxes they paid under protest, as indicated in the District Court judgement entered in accordance with the Montana Supreme Court opinion herein, respondents, in applying for a

refund, will have to recalculate their taxes based upon Senate Bill No. 335 and, in particular, section 1 thereof, Appendix, pages 3a and 4a. The whole purpose of respondents' bringing this litigation was to have the question determined as to whether the interest income from these specific federal obligations was subject to taxation under the Montana Corporation License Tax. While the Montana Supreme Court has agreed with the position of respondents that this interest income from these particular federal obligations cannot be taxed under the Montana Corporation License Tax, the passage of Senate Bill No. 335 renders this decision by the Montana Supreme Court meaningless. If respondents have previously deducted this interest income from their tax returns, they will be required under section 6 of Senate Bill No. 335 to recalculate their taxes on the basis of section 1 of this bill. If taxpayers, such as respondents, seek refunds on taxes already paid on the basis of the decision of the Montana Supreme Court herein, they will be required under section 6 of Senate Bill No. 335, to recalculate their taxes on the basis of section 1 of that bill.

Since the time of the decision by the Montana Supreme Court herein, the Montana legislature has changed the law such that if interest income from these federal obligations is excluded in any fashion, then the corporate taxpayer will lose deduction that it was previously entitled to for interest expense incurred in obtaining these tax-exempt federal obligations. Therefore, the issue as to whether the interest income from the specific federal obligations is subject to taxation under the Montana Corporation License Tax is moot because the taxpayer must either include the interest income or, if it is excluded, he must recalculate his interest expense deduction, on the basis of Senate Bill No. 335 and pay taxes on the disallowed interest expense.

Petitioner with its petition for a writ of certiorari is asking this Court to review a question that is moot due to the changes made in the Montana Corporation License Tax by the Montana legislature in light of the decision of the Montana Supreme Court herein. This Court should not grant the petition for certiorari since affirmation of the decision of the Montana

Supreme Court or reversal of that decision will have no effect upon taxes being assessed or paid in Montana under the Montana Corporation License Tax in light of the passage and approval of Senate Bill No. 335.

B. THIS COURT IS BEING ASKED TO RENDER AN ADVISORY OPINION ON THE QUESTION OF WHETHER THE MONTANA CORPORATE LICENSE TAX IS A FRANCHISE TAX WHICH EXCEEDS THE SCOPE OF THE ISSUES RAISED IN THE COURTS BELOW.

As pointed out in the petition for certiorari, on page 11 thereof, respondents never questioned the nature of the Montana Corporation License Tax as being something other than a franchise tax. Petitioner, in its answer to respondents' complaint and in its briefs filed with the Montana Supreme Court, took the position that the Montana Corporation License Tax was a franchise tax. Petitioner never took the position that, if the tax is not a franchise tax, it is at the very least a "nonproperty tax in lieu thereof imposed on corporations" which would still fall within the exception of 31 U.S.C. § 742. See, page 12 of the petition. Since there was no argument raised in the District Court of the First Judicial District of the State of Montana or in the Montana Supreme Court in this litigation as to whether the Montana Corporation License Tax was something other than a franchise tax and respondents and petitioner having never raised the question that, even if the tax was construed to be something other than a franchise tax, that it is a nonproperty tax imposed on corporations in lieu thereof, this Court is being asked to render an advisory opinion on an issue that is not in dispute between petitioner and respondents. Such a decision would exceed the scope of respondents' petition for declaratory judgement herein and would be contrary to the Montana declaratory judgement act.

It has been held, in Montana, that a court in a declaratory judgement action has no jurisdiction to determine matters purely speculative, enter anticipatory judgements, declare social status, deal with theoretical problems, give advisory opinions, answer moot questions, adjudicate academic matters, provide

for contingencies which may hereafter arise, or give abstract opinions. Mt. Dept. of Nat. Res. and Conser. v. Intake Water Company, 171 Mont. 416, 440, 558 P.2d 1110 (1976). Here, petitioners are asking this Court, as they did in their petition for rehearing to the Montana Supreme Court, to render an advisory opinion as to whether the Montana Corporation License Tax is a franchise tax, when this issue was not in dispute between the parties hereto. As was argued to the Montana Supreme Court in response to the amicus curiae briefs in support of the petition for rehearing, the duty of a court is to adjudicate actual or real controversies existing among parties with adverse interests and conflicting claims. Here, respondents and petitioner have no adverse or conflicting claim with regard to whether the Montana Corporation License Tax is a franchise tax. Their only conflicting claim is whether the interest income from the specific federal obligations involved herein can be subject to tax under the Montana Corporation License Tax. By asking this Court to rule on whether the Montana Corporation License Tax is a franchise tax or, at least, a nonproperty tax imposed on corporations in lieu thereof, petitioner is asking this Court to rule on an issue that was not in dispute between these parties and was not argued or briefed to either the Montana Supreme Court or the District Court herein. Petitioner is asking this Court to render an advisory opinion on the question of whether the Montana Corporation License Tax is a franchise tax, or a nonproperty tax imposed on corporations in lieu thereof. This Court should, therefore, deny this petition for certiorari since the issue the petitioner attempts to raise exceeds the scope of the issues raised in the courts below and petitioner is asking this Court to require respondents to argue a question that respondents cannot argue since it is their position that the Montana Corporation License Tax is a franchise tax.

C. THE MONTANA SUPREME COURT FULLY CONSIDERED THE ISSUES PRESENT HERE AND DECIDED THE SAME CORRECTLY.

The issue before the Montana Supreme Court was whether

the District Court of the First Judicial District of the State of Montana erred by deciding that interest income from certain federal obligations held by respondents was includable in net income and hence subject to the Montana Corporation License Tax. See Appendix to Petitioner's Petition, page 4a. The Montana Supreme Court recognized that the District Court had predicated its decision that this interest income was includable in net income on the basis of 31 U.S.C. § 742. The Court then went on to say:

> The District Court reasoned that the exception stated in the above federal statute applied to the Montana Corporation License Tax, which is admitted by the parties herein to be a franchise tax, and hence the interest income from the federal obligations is includable in the net income which is the basis upon which the license tax is computed.
>
> The taxpayers unsuccessfully contended in the District Court that the specific federal statutes which created the federal obligations and authorized their issuance expressly exempted both the principal and the interest paid thereon from all state taxation except estate and gift taxes. The federal statutes which created the federal obligations involved herein, authorized their issuance and contained the exemption are: 12 U.S.C. § 1433 (1976); 12 U.S.C. § 1725(e) (1976); 12 U.S.C. § 2055 (1976); 12 U.S.C. § 2079 (1976); 12 U.S.C. § 2134 (1976); and 31 U.S.C. § 769 (1976). Those federal statutes expressly provide that the principal and interest of various federal obligations are exempt from all state taxation except certain taxes not relevant here.
>
> The Department argued that the Montana Corporation License Tax is a franchise tax on the privilege of doing business in Montana with the tax based upon or measured by the net income of the taxpayer. Hence, it was argued that the tax is not on the property (interest income) but is on the privilege. This Court finds the argument to be unpersuasive. It is a distinction without a difference in our

opinion. If the franchise tax is on the privilege and the tax is based on the net income, this Court concludes that the tax is on the privilege and on the net income. If the net income includes tax exempt interest, the tax is on exempt income which is prohibited by the specific federal statutes creating the federal obligations and granting the tax exemption. The Montana Supreme Court held in 1976 in the case of Security Bank v. Connors and Colbo (1976), 170 Mont. 59, 550 P.2d 1313, that the Montana Corporation License Tax is a tax on net income. It also appears to this Court that by the Department's including the tax exempt interest in net income, the Department is seeking to tax indirectly what it cannot tax directly, in violation of the general rule set forth in Section 31 U.S.C. § 742 (1976). See Federal Products Corp. v. Norberg, (R.I. 1981), 429 A.2d 447.

First Federal Savings and Loan Association v. Department of Revenue, _____ Mont. _____, 654 P.2d 496 (1982), Appendix to Petitioner's Writ, pages 5a and 6a.

As can be seen from the above quotation, the Montana Supreme Court based its decision herein on three points. First, the Montana Supreme Court, contrary to the argument made in the petition on page 11 thereof, had held in the case of Security Bank v. Connors and Colbo, supra., that the Montana Corporation License Tax was a tax on net income. The Montana Supreme Court reached this result in Security Bank on the basis of the plain language of the corporate license tax, as set forth in section 15-31-122, Montana Code Annotated, which imposes a tax of 6¾ percent of the net income. While the Montana court recognized that the corporate license tax was a franchise tax, as conceded by the parties to this litigation, and recognized that the tax is imposed on the privilege of doing business, the Court was compelled to conclude on the basis of the plain language of the aforementioned statute that the tax was also imposed on the net income. Net income was simply not just a measuring devise for purposes of the tax, under the plain language of the Mon-

tana act. Secondly, the Montana Court recognized, as was argued to it and again contrary to the statements made in the petition on page 15 thereof, that 31 U.S.C. § 742 contained no exemptive language with regard to interest income from federal obligations until 1959 whereas the federal statutes relied upon by respondents herein have since the date of their enactment, prior to 1959, contained specific language prohibiting state taxation of the interest income from these obligations. This Court has recognized, when addressing the question of whether a franchise tax can reach interest income from certain federal obligations with specific exemptive language for the interest income similar to that involved herein, that, while franchise taxes generally can be measured by tax-exempt securities, interest income from Liberty Bonds and Federal Farm Loan Bonds cannot be included in the measure of a franchise tax since the statutes authorizing the issuance of those obligations expressly prohibit taxation of the income from those obligations. Macallen Company v. Massachusetts, 279 U.S. 620, 49 S. Ct. 432, 72 L.Ed. 874 (1929); Miller v. Milwaukee, 272 U.S. 709, 47 S. Ct. 280, 71 L.Ed. 487 (1927). This Court has also refused to grant a petition for certiorari where the sole question involved was whether interest income from Liberty Bonds, which was declared to be tax exempt from all state taxation, could be reached by a franchise tax in the District of Columbia. See, District of Columbia v. Riggs National Bank, 30 F. 2d 873 (D.C. Ct. of Appeals, 1929), cert. denied, 279 U.S. 846, 49 S.Ct. 343, 73 L.Ed. 991. Finally, the Montana Supreme Court recognized that in amending 31 U.S.C. § 742 in 1959, Congress inserted language therein prohibiting both direct and indirect taxation of interest income from federal obligations. The Montana Court then applied this direct and indirect language to the specific federal statutes involved herein, on the basis of the case of Federal Products Corp., v. Norbert, 429 A.2d 442 (R.I. 1981) and held that petitioner was attempting to indirectly tax the interest income from these federal obligations by and through a franchise tax, which was not permissible under the plain language of 31 U.S.C. § 742. It was also pointed out to the Montana Supreme Court and implicitly recognized by it in the

above quoted language, that to hold that the taxation of the interest income from these specific federal obligations by and through a franchise tax is governed by 31 U.S.C. § 742, would render the particular federal statutes involved herein meaningless. This Court has held that is is a rule of federal statutory construction that a court will not lightly conclude that a Congressional enactment has no purpose or function, but will strive to give appropriate meaning to each of the statute's provisions. Merchantile Nat. Bank v. Langdeau, 371 U.S. 555, 83 S. Ct. 520, 9 L.Ed. 2d 523; Roseto v. Wyman, 397 U.S. 397, 90 S. Ct. 1207, 25 L.Ed. 2d 442. It was respondents' position that the only way to give appropriate meaning to the statutes relied upon by them was to declare the interest income from these specific federal obligations exempt from the reach of the Montana Corporation License Tax. By asking this Court to grant the petition for certiorari and to reverse the decision of the Montana Supreme Court, petitioners are asking this Court to violate its rules of statutory construction as set forth above.

The decision of the Montana Supreme Court was proper herein since it gives effect to the statutes relied upon by respondents in this matter. The Court also recognized that, as this Court has held a number of times, where Congress has spoken on the immunity from state taxation of a federal obligation or the interest therefrom, full effect is given to this Congressional expression of immunity. Pittman v. Home Owners Loan Corp., 308 U.S. 21, 60 Sup. Ct. 15, 84 L.Ed. 16 (1939); Helvering v. Gearhardt, 304 U.S. 405, 58 Sup. Ct. 969, 82 L.Ed. 1427 (1938). The federal statutes involved herein declare that the interest income from these specific federal obligations is exempt from all state taxation. Congress has spoken as to the immunity of this interest income from state taxation. It did not put any condition on this immunity that it did not apply to franchise taxation or other nonproperty taxation in lieu thereof. Congress specifically declared this interest income to be tax exempt. If petitioner and amicus curiae believe that this interest income should be subject to franchise taxation, then this is a question for Congress to address. It was Congress which passed these

particular federal statutues declaring this interest income to be exempt from all state taxation. It can be noted that, when Congress amended 31 U.S.C. § in 1959, it did not amend these particular federal statutes although it did repeal certain other federal statutes similar to those involved herein. See P.L. 86-346, Title I, Section 105(b), 73 Stat. 622. The statutes Congress repealed were those pertaining to Second Liberty Bond issue, United States Treasury Notes, and United States Certificates of Indebtedness and Treasury Bills (other than those in question here), all of which contained provisions specifically exempting interest income from those obligations from any form of state taxation. See 31 U.S.C. § 747 (1959); 31 U.S.C. § 753 (1959); and 31 U.S.C. § 754 (1959). Congress repealed these specific exemptions at the time that it amended 31 U.S.C. § 742. Since Congress saw fit to repeal these particular statutes, which are similar to the ones involved herein, but did not feel compelled to repeal the statutes relied upon by respondents and relied upon by the Montana Supreme Court in rendering its decision herein, the only conclusion that can be reached is that Congress intended that the interest income from these particular federal obligations should continue to be exempt from all state taxation, including franchise taxation, despite the broad authorization for such taxation set forth in 31 U.S.C. § 742. If it is the intent of Congress that the interest income from the federal obligations held by respondents should be subject to franchise taxation, then Congress should so declare by amending or repealing the statutes involved herein.

CONCLUSION

For the reasons set forth above, the respondents herein submit that a writ of certiorari should not be granted in this case.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Edmund F. Sheehy, Jr., a member of the Bar of the Supreme Court of the United States and counsel of record for First Federal Savings and Loan Association of Missoula and Havre Federal Savings and Loan Association, respondents herein, hereby certify that on May 18, 1983, I served three copies of the Brief in Opposition to the Petition for Certiorari on each of the parties herein, as follows:

On Department of Revenue, State of Montana, petitioner herein, by depositing such copies in the United States Post Office, Kalispell, Montana, with first class postage prepaid, properly addressed to the post office address of Michael J. Rieley, the above named petitioner's counsel of record, at Mitchell Building, Helena, Montana, 59620.

On the amicus curiae herein, by depositing such copies in the United States Post Office, Kalispell, Montana, with first class postage prepaid, properly addressed to the post office address of John Van deCamp, Attorney General of California, the counsel of record for amicus curiae, at 3580 Wilshire Boulevard, Los Angeles, California, 90010, and William D. Dexter, General Counsel, Multistate Tax Commission, 204 Custer Way, Tumwater, Washington, 98501.

All parties required to be served have been served.

DATED May 18, 1983.

Edmund F. Sheeehy, Jr.
CANNON & SHEEHY
2031 Eleventh Avenue
Helena, MT 59601

Office-Supreme Court, U.S.
FILED
MAY 20 1983
ALEXANDER L. STEVAS,
CLERK

No. 82-1471

In The

Supreme Court of the United States

October Term, 1982

THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATON,

Respondents.

APPENDIX

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APPENDIX

SENATE BILL NO. 335
INTRODUCED BY TOWE, ET AL.

A BILL FOR AN ACT ENTITLED: "AN ACT TO DISALLOW DEDUCTIONS RELATED TO EXCLUDED INTEREST INCOME FOR MONTANA CORPORATION LICENSE TAX PURPOSES; TO APPLY THE DISALLOWANCE DEDUCTION RETROACTIVELY TO ALL TAXABLE PERIODS DURING WHICH SUCH INCOME IS EXCLUDED FROM GROSS INCOME: PROHIBITING CONSOLIDATED RETURNS FOR FINANCIAL INSTITUTIONS UNDER THE CORPORATE LICENSE TAX; REAFFIRMING THE INCLUSION OF STATE AND LOCAL BOND INCOME IN THE DEFINITION OF NET INCOME FOR CORPORATION LICENSE TAX PURPOSES; AND PROVIDING AN IMMEDIATE EFFECTIVE DATE AND APPLICABILITY DATES."

WHEREAS, the Montana Corporation License Tax Act (Title 15, chapter 31, part 1) was intended, after the enactment of Chapter 634, Laws of 1979, to require all corporations to report and pay a tax upon all income derived from obligations of the United States or its agencies or instrumentalities as permitted by Title 31, section 742, United States Code; and

WHEREAS, the Montana Supreme Court on September 23, 1982 (petition for rehearing denied December 6, 1982), decided in the case cited below that such income must be excluded from the measure of the subject tax; and

WHEREAS, the Legislature disagrees with the Montana Supreme Court's decision in the case of First Federal Savings and Loan Association, a Federally Chartered Association, et al., Plaintiffs and Appellants v. Department of Revenue, et al., Defendants and Respondents, Cause No. 81-528, and has filed through its Revenue Oversight Committee, an Amicus Curiae brief in support of the position of the Department of Revenue; and

WHEREAS, the Department of Revenue is presently seeking to have the United States Supreme Court review the matter, and at this time other decisions are also being reviewed by the United States Supreme Court that might have a bearing on the issue of the taxability of such income; and

WHEREAS, in the interim uncertainty exists as to the taxability of such income and claims for refund of tax and returns of income will be made by corporations based upon the exclusion of such income; and

WHEREAS, the Legislature desires to maintain approximately the current level of revenue to state and local government; and

WHEREAS, immediate legislative action is necessary.

THEREFORE, it is the intent of the Legislature to proportionately reduce the allowable deductions to all corporations for all taxable periods for which interest income is excluded or claim for refund of tax is made upon such exclusion under claim of right under federal law.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

Section 1. Reduction of deductions relating to excluded income. (1) A corporation, taxable under Title 15, chapter 31, part 1, that excludes interest from gross income which would be taxable except for federal law which must adjust its allowable deductions for all taxable periods for which interest is excluded in the following manner:

(a) the total amount of interest excluded from gross income by federal law must be determined;

(b) the total amount of all interest income from all sources must be determined;

(c) the ratio of excluded interest income to all interest income

must be determined; and

(d) the total deductions allowable under 15-31-114 must be reduced by an amount determined by multiplying the amount of deduction otherwise allowable by the ratio of excluded interest to all interest income; however, the product of this calculation may not exceed the amount of excluded interest income.

(2) Allowable deduction must be reduced with respect to all corporations that exclude interest income otherwise taxable upon returns filed for all taxable periods for which such exclusion is claimed and for all taxable periods for which a claim for refund is made.

THERE IS A NEW MCA SECTION THAT READS:

Section 2. Consolidate returns prohibited. (1) A majority of the corporation license tax collected from financial institutions is paid to local government areas in which each financial institution is located. However, consolidated returns for financial institutions do not reflect the true tax attributable to each local government. In addition, consolidated returns would permit financial institutions to offset income against losses of nonfinancial institutions, thereby distorting the true income of each financial organization.

(2) In accordance with subsection (1), financial institutions are prohibited from filing consolidated returns under 15-31-141.

THERE IS A NEW MCA SECTION THAT READS:

Section 3. Reaffirmation of bond income inclusion in definition of net income for corporation license tax purposes. Notwithstanding the provisions of any other law, the income from bonds or other obligations issued by any state or political subdivision of a state are included in gross and net income for purposes of the corporation license tax. Further, such income has been included in gross and net income since the effective date of Chapter 634, Laws of 1979, which law repealed the exclusion of

such income from the tax base of the corporation license tax.

Section 4. Codification instructions. Sections 1 through 3 are intended to be codified as integral parts of Title 15, chapter 31, part 1.

Section 5. Severability. If a part of this act is invalid, all valid parts that are severable from the invalid part remain in effect. If a part of this act is invalid on one or more of its applications, the part remains in effect in all valid applications that are severable from the invalid applications.

Section 6. Effective date — applicability dates. This act is effective on passage and approval. Sections 1 and 3 of this act apply retroactively, within the meaning of 1-2-109, to taxable periods beginning on and after December 31, 1978 (the effective date of Chapter 634, Laws of 1979), for which a corporation has excluded interest income based upon federal law or for which a corporation has included interest income and subsquently claims a refund of taxes paid based upon federal law. Section 2 of this act applies to taxable periods beginning after December 31, 1982.

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No. 82-1471

In The
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October Term, 1982

THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION,

Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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No. 82-1471

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FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION,

Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

This Reply Brief is submitted to the Court pursuant to Supreme Court Rule 22.5 in answer to Respondents' Brief in Opposition to Petition for a Writ of Certiorari to the Supreme Court of Montana.

This case concerns the correctness of the interpretation given to the following federal statutes by the Montana Supreme Court: 31 U. S. C. §§ 742[1], 649; 12 U. S. C. §§ 1433, 1725(e), 2055, 2079, and 2134. All of these statutes pertain to federal obligations and each contains exemptions

[1]Now Recodified as 31 U. S. C. § 3124, *See*, Brief of Amici Curiae in Support of Petition for Certiorari, at pp. 4-5, fn. 1.

regarding state taxation as well as particular exceptions thereto.

Pursuant to this Court's request, Respondents filed a Brief in Opposition to Certiorari and raised the following arguments:

(1) Enactment of Montana Senate Bill No. 335 has rendered the Petition for Certiorari and issue contained therein moot.

(2) This Court has been requested to render an advisory opinion in this matter.

(3) The Montana Supreme Court correctly interpreted the federal statutes underlying the issue presented for review.

To the extent that these assertions are raised for the first time, Petitioner will now address them.

I.

The issue in this matter is the interpretation of Federal Statutes and the Montana Legislative Enactment does not render it moot.

The 1983 Montana Legislature enacted Senate Bill No. 335 in response to the Montana Supreme Court's decision in this matter.[2] See, Petitioner's Reply Appendix,

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[2]Respondents' Appendix contains a version of the Bill prior to enrollment and signature. Therefore Petitioner has included in this Reply Brief a signed copy of the Enrolled Bill.

App. 4-5. Since the Montana Legislature meets only once every two years, prophylactic action was needed to ensure preservation and continuity of the state's tax revenue base. However, as written, the new law does not affect the matter now before this Court either as to parties, subject matter, or issue for review. At this point of time, the new law, although currently effective, is not applicable to the present matter. The recent enactment applies only when federal law precludes state taxation of interest income. In the present matter this question, i. e., whether federal law prohibits inclusion of interest income in the measure of a nondiscriminatory franchise tax, has not been yet definitively answered. Consequently the matter and issue presented to this Court in both the Petition of the State of Montana and the Brief of the Amici Curiae is not moot.

The new statute provides a formula for proportionate disallowance of deductions attributable to interest income that is excludable from the measurement base of the Montana corporation license tax because of federal law. See, Petitioner's Reply Appendix, App. 6-7. The Respondents base their assertion of mootness on an erroneous reading of the new law. Respondents describe the new law in their Brief in Opposition to Certiorari at p. 7:

> Since the time of the decision by the Montana Supreme Court herein, the Montana legislature has changed the law such that *if interest income from these federal obligations is excluded in any fashion,* then the corporate taxpayer will lose deduction [sic] that it was previously entitled to for interest expense incurred in obtaining these tax-exempt federal obligations. Therefore, the issue as to whether the interest income from the specific federal obligations is subject to taxation under the Montana Corporation

> License Tax is moot because the taxpayer must either include the interest income or, if it is excluded, he must recalculate his interest expense deduction, on the basis of Senate Bill No. 335 and pay taxes on the disallowed interest expense. (Emphasis added.)

The Respondents assert that a corporation which excludes interest income for any reason must also reduce its deductions in conformance with the new formula. In short, Respondents indicate to this Court that such a taxpayer has a voluntary option to either, (1) include the interest income in the measurement and receive all of its deductions or (2) exclude interest income and decrease its deductions accordingly.

Contrary to Respondents' assertion, there exists no such option for the taxpayer per the express words of the new law. The emphasized language from Respondents' brief, supra, constitutes an incorrect paraphrasing of the new law. The key language of the new law is as follows:[3]

> Section 1. Reduction of deductions related to excluded income. (1) A corporation, taxable under Title 15, chapter 31, part 1, that excludes interest from gross income *which would be taxable except for federal law* must adjust its allowable deductions for all taxable periods for which interest is excluded in the following manner: . . . (Emphasis added.)

The operative words are those emphasized. As can be readily ascertained, the formula for reduction of deductions is applicable *only* in instances where interest income has been determined not to be includable in the income measure of the Montana Corporation License Tax.

---

[3]See, Petitioner's Reply Brief, Appendix, App. 5.

The triggering mechanism for the new law to be operable in the present matter is for the Petitioner to receive an adverse decision from this Court. Only at that time would the new law be applicable. Conversely, if the position of the Petitioner is determined to be correct then the formula would never be applicable to the instant case. Respondents' allegations of mootness is substantively fallacious per the express words of the new legislative enactment.

The new legislation does not affect the situation presented to this Court for review. See, *Bullock v. Carter*, 405 U. S. 134 (1972), *Brockington v. Rhodes*, 396 U. S. 41 (1969), and *Hunter v. Erickson*, 393 U. S. 385 (1969).

The Court should recognize that the result of this case is also not moot. Although the Montana Legislature provided a statutory mechanism to minimize the overall effect of loss of tax revenue in the event the decision of the Montana Supreme Court is upheld by this Court[4] the formula does not operate so as to result in a complete wash.

Preliminary calculations demonstrate that the State would collect less tax revenue under the offset of deductions formula. Thus there are actual dollars at stake for both the taxpayers and the Petitioner. Since the tax effect is not the same, both parties will be significantly affected by this Court's ultimate decision of the issue presented.

---

[4]See, preamble to S. B. 355, Petitioner's Reply Appendix, App. 4-5.

II.

This Court is not being asked to issue an advisory opinion.

Petitioner agrees with the Respondents' characterization of the Montana Corporation License Tax as stated in Respondents' Brief in Opposition to Certiorari, at p. 9:

> *Here, respondents and petitioner have no adverse or conflicting claim with regard to whether the Montana Corporation License Tax is a franchise tax.* Their only conflicting claim is whether the interest income from the specific federal obligations involved herein can be subject to tax under the Montana Corporation License Tax. (Emphasis added.)

Petitioner is not requesting this Court to definitively affirm the characterization of the tax, as that has already been done by the Montana Supreme Court, in its rightful province, *see*, Petition for Certiorari, pp. 11-12.

As framed in the Petition for Certiorari at p. i., the question presented for review concerns: (1) whether the Montana tax satisfies the exception contained in 31 U. S. C. § 742 and (2) whether the immunity described in certain federal statutes providing for issuance of certain federal obligations is broader than that provided by 31 U. S. C. § 742. Clearly, Petitioner is not asking for an advisory opinion.

III.

The last argument raised by Respondents goes to the merits of this case and is more appropriate under the Rules of this Court to be addressed in briefing on the merits.

CONCLUSION

As Petitioner has demonstrated, the issue presented to this Court for review is not moot. Because of the import of this viable question to the Petitioner and the 25 states appearing as *Amici*, the Court is urged to grant plenary consideration and resolve the issue.

Respectfully submitted,

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APPENDIX

CHAPTER NO. 673

SENATE BILL NO. 335

INTRODUCED BY TOWE, TURNAGE, FABREGA, YARDLEY, WILLIAMS, MARKS, RAMIREZ, ABRAMS, THOMAS, ASAY, BLAYLOCK, GOODOVER, McCALLUM, KOLSTAD, HARRINGTON, NEUMAN, ZABROCKI, DONALDSON, SEVERSON, CHRISTIAENS, KITSELMAN, NORDTVEDT

IN THE SENATE

February 1, 1983	Introduced and referred to Committee on Taxation.
February 2, 1983	Fiscal Note requested.
February 8, 1983	Fiscal Note returned.
February 23, 1983	Committee recommend bill do pass. Report adopted.
February 28, 1983	Bill printed and placed on members' desks.
March 1, 1983	Second reading, do pass.
March 2, 1983	Correctly engrossed.
March 3, 1983	Third reading, passed. Ayes, 48; Noes, O. Transmitted to House.

IN THE HOUSE

March 7, 1983	Introduced and referred to Committee on Taxation.
March 23, 1983	Committee recommend bill be concurred in as amended. Report adopted.
March 26, 1983	Second reading, concurred in as amended.
	Third reading, concurred in.

IN THE SENATE

March 29, 1983	Returned to Senate with amendments.
April 8, 1983	Second reading, amendments concurred in.
April 11, 1983	Third reading, amendments concurred in. Ayes, 50; Noes, 0.
	Sent to enrolling.
April 13, 1983	Correctly enrolled.
	Signed by President.
April 14, 1983	Signed by Speaker.
April 15, 1983	Delivered to Governor.
April 20, 1983	Returned from Governor with recommended amendments.
	Second reading, Governor's amendments not concurred in.

IN THE HOUSE

April 20, 1983	Governor's amendments transmitted to House.
April 21, 1983	On motion of April 20, 1983, Governor's amendments placed on second reading this day.
	Second reading, Governor's amendments concurred in.
	Third reading, Governor's amendments concurred in.

IN THE SENATE

April 21, 1983	On motion, Free Conference Committee requested and appointed.
	Free Conference Committee reported.

Second reading, Free Conference Committee report rejected. Ayes 26; Noes, 23.

Free Conference Committee dissolved.

On motion, new Free Conference Committee requested and appointed.

New Free Conference Committee dissolved.

On motion, second new Free Conference Committee requested and appointed.

Second new Free Conference Committee reported.

Second reading, second new Free Conference Committee report rejected. Ayes, 35; Noes, 15.

Second new Free Conference Committee report rejected by House.

IN THE SENATE

April 21, 1983 — Returned to Senate. Sent to enrolling.

Returned to Governor for further consideration.

AN ACT TO DISALLOW DEDUCTIONS RELATED TO EXCLUDED INTEREST INCOME FOR MONTANA CORPORATION LICENSE TAX PURPOSES; TO APPLY THE DISALLOWANCE OF DEDUCTION RETROACTIVELY TO ALL TAXABLE PERIODS DURING WHICH SUCH INCOME IS EXCLUDED FROM GROSS INCOME; PROHIBITING CONSOLIDATED RETURNS FOR FINANCIAL INSTITUTIONS UNDER THE CORPORATE LICENSE TAX; REAFFIRMING THE INCLUSION OF STATE AND LOCAL BOND INCOME IN

THE DEFINITION OF NET INCOME FOR CORPORATION LICENSE TAX PURPOSES; AND PROVIDING AN IMMEDIATE EFFECTIVE DATE AND APPLICABILITY DATES.

WHEREAS, the Montana Corporation License Tax Act (Title 15, chapter 31, part 1) was intended, after the enactment of Chapter 634, Laws of 1979, to require all corporations to report and pay a tax upon all income derived from obligations of the United States or its agencies or instrumentalities as permitted by Title 31, section 742, United States Code; and

WHEREAS, the Montana Supreme Court on September 23, 1982 (petition for rehearing denied December 6, 1982), decided in the case cited below that such income must be excluded from the measure of the subject tax; and

WHEREAS, the Legislature disagrees with the Montana Supreme Court's decision in the case of *First Federal Savings and Loan Association, a Federally Chartered Association, et al., Plaintiffs and Appellants v. Department of Revenue, et al., Defendants and Respondents,* Cause No. 81-528, and has filed, through its Revenue Oversight Committee, an *Amicus Curiae* brief in support of the position of the Department of Revenue; and

WHEREAS, the Department of Revenue is presently seeking to have the United States Supreme Court review the matter, and at this time other decisions are also being reviewed by the United States Supreme Court that might have a bearing on the issue of the taxability of such income; and

WHEREAS, in the interim uncertainty exists as to the taxability of such income and claims for refund of

tax and returns of income will be made by corporations based upon the exclusion of such income; and

WHEREAS, the Legislature desires to maintain approximately the current level of revenue to state and local government; and

WHEREAS, immediate legislative action is necessary.

THEREFORE, it is the intent of the Legislature to proportionately reduce the allowable deductions to all corporations for all taxable periods for which interest income is excluded or claim for refund of tax is made upon such exclusion under claim of right under federal law.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

Section 1. Reduction of deductions related to excluded income. (1) A corporation, taxable under Title 15, chapter 31, part 1, that excludes interest from gross income which would be taxable except for federal law must adjust its allowable deductions for all taxable periods for which interest is excluded in the following manner:

(a) the total amount of interest excluded from gross income by federal law must be determined;

(b) the total amount of all interest income from all sources must be determined;

(c) the ratio of excluded interest income to all interest income must be determined; and

(d) the total deductions allowable under 15-31-114 must be reduced by an amount determined by multiplying the amount of deduction otherwise allowable by the ratio

of excluded interest to all interest income; however, the product of this calculation may not exceed the amount of excluded interest income.

(2) Allowable deductions must be reduced with respect to all corporations that exclude interest income otherwise taxable upon returns filed for all taxable periods for which such exclusion is claimed and for all taxable periods for which a claim for refund is made.

Section 2. Consolidated returns prohibited. (1) A majority of the corporation license tax collected from financial institutions is paid to local government areas in which each financial institution is located. However, consolidated returns for financial institutions do not reflect the true tax attributable to each local government. In addition, consolidated returns would permit financial institutions to offset income deductions for all taxable periods for which interest is excluded in the following manner:

(a) the total amount of interest excluded from gross income by federal law must be determined;

(b) the total amount of all interest income from all sources must be determined;

(c) the ratio of excluded interest income to all interest income must be determined; and

(d) the total deductions allowable under 15-31-114 must be reduced by an amount determined by multiplying the amount of deduction otherwise allowable by the ratio of excluded interest to all interest income; however, the product of this calculation may not exceed the amount of excluded interest income.

(2) Allowable deductions must be reduced with respect to all corporations that exclude interest income otherwise taxable upon returns filed for all taxable periods for which such exclusion is claimed and for all taxable periods for which a claim for refund is made.

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(2) In accordance with subsection (1), financial institutions are prohibited from filing consolidated returns under 15-31-141.

Section 3. Reaffirmation of bond income inclusion in definition of net income for corporation license tax purposes. Notwithstanding the provisions of any other law, the income from bonds or other obligations issued by any state or political subdivision of a state are included in gross and net income for purposes of the corporation license tax. Further, such income has been included in gross and net income since the effective date of Chapter 634, Laws of 1979, which law repealed the exclusion of such income from the tax base of the corporation license tax.

Section 4. Codification instruction. Sections 1 through 3 are intended to be codified as integral parts of Title 15, chapter 31, part 1.

Section 5. Severability. If a part of this act is invalid, all valid parts that are severable from the invalid part remain in effect. If a part of this act is invalid in one or more of its applications, the part remains in effect in all valid applications that are severable from the invalid applications.

Section 6. Effective date—applicability dates. This act is effective on passage and approval. Sections 1 and 3 of this act apply retroactively, within the meaning of 1-2-109, to taxable periods beginning on and after December 31, 1978 (the effective date of Chapter 634, Laws of 1979), for which a corporation has excluded interest income based upon federal law or for which a corporation has included interest income and subsequently claims a refund of taxes paid based upon federal law. Section 2 of this act applies to taxable periods beginning after December 31, 1982.

I hereby certify that the within bill originated in the Senate.

/s/ John W. Larson
Secretary of the Senate

/s/ Stanley D. Stephens
President of the Senate
Signed this 28th day of April, 1983.

/s/ Daniel Kemmis
Speaker of the House
Signed this 28th day of April, 1983.

CHAPTER NO. 673

SENATE BILL NO. 335

INTRODUCED BY TOWE, TURNAGE, FABREGA, YARDLEY, WILLIAMS, MARKS, RAMIREZ, ABRAMS, THOMAS, ASAY, BLAYLOCK, GOODOVER, McCALLUM, KOLSTAD, HARRINGTON, NEUMAN, ZABROCKI, DONALDSON, SEVERSON, CHRISTIAENS, KITSELMAN, NORDTVEDT

AN ACT TO DISALLOW DEDUCTIONS RELATED TO EXCLUDED INTEREST INCOME FOR MONTANA CORPORATION LICENSE TAX PURPOSES; TO APPLY THE DISALLOWANCE OF DEDUCTION RETROACTIVELY TO ALL TAXABLE PERIODS DURING WHICH SUCH INCOME IS EXCLUDED FROM GROSS INCOME; PROHIBITING CONSOLIDATED RETURNS FOR FINANCIAL INSTITUTIONS UNDER THE CORPORATE LICENSE TAX; REAFFIRMING THE INCLUSION OF STATE AND LOCAL BOND INCOME IN THE DEFINITION OF NET INCOME FOR CORPORATION LICENSE TAX PURPOSES; AND PROVIDING AN IMMEDIATE EFFECTIVE DATE AND APPLICABILITY DATES.

This bill was received by the Governor this 29th day of April, 1983.

/s/Ted Schwinden
Governor

By /s/ Martha Wahlstrand
Approved 4/29/83
/s/Ted Schwinden
Governor

STATE OF MONTANA
Filed May 2, 1983
Jim Waltermire
Secretary of State

By /s/ Marian F. Campbell
Deputy

Office-Supreme Court, U.S.
FILED
APR 4 1983
ALEXANDER L. STEVAS,
CLERK

No. 82-1471

In The

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Petitioner,

vs.

FIRST FEDERAL SAVINGS AND LOAN ASSOCIATION OF MISSOULA, AND HAVRE FEDERAL SAVINGS AND LOAN ASSOCIATION,

Respondents.

BRIEF OF THE STATES OF ALABAMA, ALASKA, ARKANSAS, CALIFORNIA, CONNECTICUT, DELAWARE, FLORIDA, HAWAII, IDAHO, IOWA, LOUISIANA, MAINE, MASSACHUSETTS, MINNESOTA, NORTH DAKOTA, OHIO, OKLAHOMA, RHODE ISLAND, SOUTH DAKOTA, TEXAS, UTAH, VERMONT, WEST VIRGINIA, WISCONSIN, AND WYOMING AS AMICI CURIAE IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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No. 82-1471

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I. INTRODUCTORY STATEMENT

Pursuant to United States Supreme Court Rule 36.1, the signatory states submit this Brief as *Amici Curiae* in support of the Petition for a Writ of Certiorari in the above-captioned case (docketed March 4, 1983, 51 U. S. L. W. 3669). Since this Brief is being sponsored and filed

by the aforementioned states, consent to its filing is not required. United States Supreme Court Rule 36.4.

II. OPINIONS BELOW

The Opinion of the Supreme Court of the State of Montana is reported at — Mont. —, 654 P. 2d 496 (1982). Copies of the Opinion, the Supreme Court of Montana's denial for a petition for rehearing, and the unreported Opinion of the District Court for the First Judicial District of the State of Montana are contained in Petitioner's Appendix, pp.: 1a-27a.

III. INTEREST OF AMICI CURIAE

The interest of the states joined as Amici in this Brief revolve around what is believed to be the far reaching effects of the opinion of the Montana Supreme Court as it relates to the question of including federal obligations within the measurement of a state franchise tax.

The finding of the Montana Supreme Court that a nondiscriminatory franchise tax may not include within its measure interest income from federal obligations, clearly has serious consequences for states other than Montana. As the argument contained herein will demonstrate, such a position is not consistent with the previous decisions of this Court. It is essential that this Court agree to hear this Petition so as to provide guidance to states in this area.

IV. ARGUMENT

It is apparent from a reading of the Petition that the Montana tax, Sections 15-31-101 and 15-31-143 (1), Montana Code Annotated, see Petition, p. 3, constitutes a nondiscriminatory franchise or other nonproperty tax imposed on corporations. As such, this Brief will only discuss that portion of the petition specifically relating to the interpretation to be given to the exemption language contained in the federal statutes.

Congress and this Court have set certain standards which limit the ability of a state to subject federal obligations to either property or franchise taxes. Since the enactment of 31 U. S. C. § 742 in 1862, this legislation contained the parameters under which states could tax federal obligations. The statute as originally enacted provided as follows: "All stocks, bonds, and other securities of the United States held by individuals, corporations, or associations within the United States shall be exempt from taxation by or under state authority." In interpreting that prohibition, this Court found specifically that the exemption contained therein did not prohibit a state from including federal interest income within the measure of a franchise tax. *Society for Savings v. Coite*, 6 Wall. 594 (1867); *Provident Institution for Savings v. Massachusetts*, 6 Wall. 611 (1867); *Hamilton Co. v. Massachusetts*, 6 Wall. 632 (1867). As countenanced by this Court a nondiscriminatory franchise tax, which constituted a tax on the privilege of doing business and not a tax on the income, could include within its measure the interest from federal obligations. Effectively, the income which could

not be taxed directly because of the prohibition contained in Section 742,[1] could be included indirectly[2] in a franchise tax.

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[1]Revised and recodified as 31 U.S.C. § 3124 on September 13, 1982 by P. L. 97-258 as follows:

§ 3124. *Exemption from taxation.*

(a) Stocks and obligations of the United States Government are exempt from taxation by a State or political subdivision of a State. The exemption applies to each form of taxation that would require the obligation, the interest on the obligation, or both, to be considered in computing a tax, except—

(1) a nondiscriminatory franchise tax or another nonproperty tax instead of a franchise tax, imposed on a corporation; and

(2) an estate or inheritance tax.

(b) The tax status of interest on obligations and dividends, earnings, or other income from evidences of ownership issued by the Government or an agency and the tax treatment of gain and loss from the disposition of those obligations and evidences of ownership is decided under the Internal Revenue Code of 1954 (26 U. S. C. 1 et seq.). An obligation that the Federal Housing Administration had agreed, under a contract made before March 1, 1941, to issue at a future date, has the tax exemption privileges provided by the authorizing law at the time of the contract. This subsection does not apply to obligations and evidences of ownership issued by the District of Columbia, a territory or possession of the United States, or a department, agency, instrumentality, or political subdivision of the District, territory, or possession.

[2]The Judiciary Report of the House of Representatives No. 97-651 (July 21, 1982), explains the purpose of the revision at p. 3:

Purpose.—The purpose of the bill is to restate in comprehensive form, without substantive change, certain general and permanent laws related to money and finance and to enact those laws as title 31, United States Code. In the restatement, simple language has been substituted for

(Continued on next page)

In 1959, Congress amended Section 742 so as to incorporate into the body of the statute itself the interpretation of it as given by this Court. Added in the 1959 amendment was the second sentence so that Section 742 reads in its entirety as follows:

> *Exemption from taxation.* Except as otherwise provided by law, all stocks, bonds, Treasury notes, and other obligations of the United States, shall be exempt from taxation by or under State or municipal or local authority. This exemption extends to every form of taxation that would require that either the obligations or the interest thereon, or both, be considered, directly or indirectly, in the computation of the tax, except nondiscriminatory franchise or other nonproperty taxes in lieu thereof imposed on corporations and except estate or inheritance taxes.

Since 1959, both by the interpretation of Section 742, as well as by Congressional mandate, any state which levied a nondiscriminatory franchise tax could include therein interest from federal obligations.

The problem in this case arises however, because of certain language contained in statutes creating certain

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(Continued from previous page)

> awkward and obsolete terms, and superseded, executed, and obsolete laws have been eliminated.

as well as substantive changes from § 742 at p. 94:

> In subsection (a), before clause (1), the words "Except as otherwise provided by law, all . . . bonds, Treasury notes, and other" are omitted as surplus. The words "political subdivision of a State" are substituted for "municipal or local authority" for clarity and consistency. The word "applies" is substituted for "extends" for clarity. *The words "directly or indirectly" are omitted as surplus.* In clause (1), the word "instead" is substituted for "in lieu" for clarity. (Emphasis added.)

federal obligations, *i. e.*, 31 U. S. C. § 769 (United States Treasury Bills); 12 U. S. C. § 1433 (Federal Home Loan Bank Notes), 1725 (e) (Federal Savings and Loan Insurance Corporation Notes), 2055 (Federal Land Bank Obligations), 2079 (Federal Farm Credit Bank Securities), and 2134 (Federal Home Loan Stock Dividends), which prohibits this particular federal income from being included within any form of state taxation. As noted in the Petition, this Court in *Memphis Bank & Trust Company v. Riley C. Garner*, — U. S. —, 51 U. S. L. W. 4104, 4105 (January 1983), at footnote 5 identified the exact issue presented here, as one which has never been addressed by it:

> In establishing the Federal Credit Bank, Congress made clear that the obligations of these banks would be immune from taxation by the States. 12 U. S. C. Sections 2055, 2079, and 2134. We have no occasion to determine whether the immunity described in these provisions is broader than that otherwise provided by 31 U. S. C. Section 742. . . .

Now this Court can specifically address this issue and find, as urged by the Petitioner, that the exemption language contained in the specific statutes does not preclude a state from including within the measure of a nondiscriminatory franchise tax, that specific federal interest income.

As the Petition has pointed out, the ability of states to tax either directly, or indirectly through a franchise or other nonproperty tax, federal interest income has in recent years come under continued question. A form of tax known as a "bank shares tax" is one method utilized by states to tax financial institutions and includes within

the base of the tax federal obligations themselves. Two cases are presently before the court, *Bank of Texas v. Childs,* 615 S. W. 2d 810 (Tex. 1981), cert. granted sub. nom. and *Bartow County Bank v. Bartow County Board of Tax Assessors,* 285 S. E. 2d 920 (Ga. 1982), appeal docketed No. 81-1834, (April 5, 1982), which directly address the question of whether or not federal obligations may be included in a bank shares tax. Since this Court has agreed to decide those cases, states which have elected that method of taxation will have definitive guidance on the question.

Other states, including the *Amici,* have elected to include the value of federal obligations within the measure of a franchise tax. As a result of the recent decision of this Court in *Memphis Bank & Trust Company, supra,* the states realize that in order to be permissible a franchise tax must be nondiscriminatory. With the present case comes a more fundamental issue: notwithstanding that a state levies a nondiscriminatory franchise or other non-property tax in lieu thereof on corporations, does the tax exempting language contained in certain statutes of issuance preclude a state from including federal interest income within the measure of a franchise tax?

This issue affects not just the State of Montana, but affects all states attempting to enact permissible franchise tax legislation which includes federal interest income in its measure without violating Congressional guidelines.

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V. CONCLUSION

This issue is of vital concern to the *Amici* and represents a question having nationwide impact in the field of state taxation. Therefore, we urge this Court to grant the Petition for a Writ of Certiorari in the present case and give plenary consideration to the matter.

Respectfully submitted,

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MOTION TO FILE BRIEF OF AMICUS CURIAE OF THE MULTISTATE TAX COMMISSION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF MONTANA

BRIEF OF AMICUS CURIAE OF THE MULTISTATE TAX COMMISSION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF MONTANA

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The Multistate Tax Commission hereby requests permission to file the attached *amicus curiae* brief. This brief is filed in support of the Montana Department of Revenue's Petition for a Writ of Certiorari to the Supreme Court of Montana in the captioned matter for the reasons stated therein.

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STATEMENT OF INTEREST

The Multistate Tax Commission (hereinafter referred to as the MTC) is the official administrative agency of the Multistate Tax Compact (hereinafter referred to as the Compact) entered into currently by 19 states and the District of Columbia as full members, and by 11 states

as associate members.[1] The purposes of the Compact are to:

1. Facilitate proper determination of state and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.

2. Promote uniformity or compatability in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.

4. Avoid duplicate taxation.[2]

In fulfillment of these objectives, the MTC has sought uniform and rational interpretations of laws which are of general concern to the states.

The MTC is vitally interested that this Court grant the Writ of Certiorari requested by the Petitioner, The Department of Revenue of the State of Montana. In the MTC's judgment, the Montana Supreme Court's decision

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[1]The current regular members are the states of Alaska, Arkansas, California, Colorado, Hawaii, Idaho, Kansas, Michigan, Missouri, Montana, Nebraska, New Mexico, North Dakota, Oregon, South Dakota, Texas, Utah, Washington and West Virginia. The associate members are the states of Alabama, Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Pennsylvania and Tennessee.

[2]The constitutionality of the Compact was upheld by the United States Supreme Court in *United States Steel Corp. v. Multistate Tax Comm'n*, 434 U. S. 452 (1978), *aff'g* 417 F. Supp. 795 (S.D.N.Y. 1976). The Court there noted that the Compact "symbolized the recognition that, as applied to multistate businesses, traditional state tax administration was inefficient and costly to both state and taxpayer." *Id.* at 456.

in *First Federal Savings and Loan Association v. Department of Revenue*, — Mont. —, 654 P. 2d 496 (1982) is clearly wrong. The Montana Supreme Court erroneously held that the Montana Corporate License Tax does not constitute a "franchise or other nonproperty tax in lieu thereof imposed on corporations" within the meaning of 31 U.S.C. § 742[3] and comparable statutes. If the tax imposed by Montana Code Annotated (MCA) § 15-31-101 is not such a tax, it is impossible to imagine how any such tax could be described and imposed by any state legislature. The MTC therefore respectfully submits that this Court should grant the Petition for Writ of Certiorari to review the Montana Supreme Court's unprecedented interpretation and application of 31 U.S.C. § 742. Otherwise, 31 U.S.C. § 742 and comparable statutes will be subject to differing interpretations which directly conflict with all the prior decisions of this Court.

———o———

ARGUMENT

The Montana Supreme Court has consistently held that the Corporate License Tax imposed by MCA § 15-31-101 is a franchise tax for the privilege of doing business in Montana in a corporate capacity. *Montana Bank v. Casey*, 135 Mont. 104, 337 P. 2d 935 (1959); *State v. J. C. Maguire Const. Co.*, 113 Mont. 324, 125 P. 2d 433 (1942).

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[3]*As of Sept. 13, 1982, this section has been revised and recodified in 31 U. S. C. Section 3124.*

This Court has traditionally held that interest from exempt federal obligations may be included in the measure of a corporate franchise tax within the limitations of 31 U.S.C. § 742. See *Werner Machine Co. v. Director of Division of Taxation*, 350 U. S. 492 (1956); *Pacific Co. v. Johnson*, 285 U. S. 480 (1932); *Education Films Corporation v. Ward*, 282 U. S. 379 (1931); *Flint v. Stone Tracy Co.*, 220 U. S. 107 (1911); *Cleveland Trust Co. v. Landers*, 184 U. S. 111 (1902); *Home Insurance Company v. New York*, 134 U. S. 594 (1890); *Society for Savings v. Coite*, 73 U. S. (6 Wall.) 594 (1867); *Provident Institution v. Massachusetts*, 73 U. S. (6 Wall.) 611 (1867); *Hamilton Co. v. Massachusetts*, 73 U. S. (6 Wall.) 632 (1867).

Nevertheless, the Montana Supreme Court held that 31 U.S.C. § 742 and comparable statutes prevented Montana from including interest income which the respondents (federal savings and loan associations) received from tax exempt federal obligations in the measure of the Montana Corporate Franchise Tax. This interpretation of either MCA § 15-31-101 or 31 U. S. C. § 742 conflicts with a long line of decisions of this Court, as cited in the preceding paragraph.

This interpretation also conflicts with the basic assumption concerning the scope of 31 U. S. C. § 742 and comparable statutes on which this Court predicated its January 24, 1983 decision in *Memphis Bank & Trust Co. v. Riley C. Garner*, — U. S. —, 51 U.S.L.W. 4104; namely, that interest income from exempt federal obligations may be included in the measure of a nondiscriminatory franchise tax.

CONCLUSION

For the above reasons, and as more fully set forth in the Writ of Certiorari filed by the Department of Revenue for the State of Montana, this Court should grant a Writ of Certiorari in this cause to review the judgment of the Montana Supreme Court.

Respectfully submitted,

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